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1998 SURVEY OF RECENT DEVELOPMENTS IN INDIANA LAW

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Cynthia Adams
Joseph R. Alberts
Kevin W. Betz
A. Richard M. Blaiklock
Joseph C. Bowman
Christopher A. Brown
Jeffrey O. Cooper
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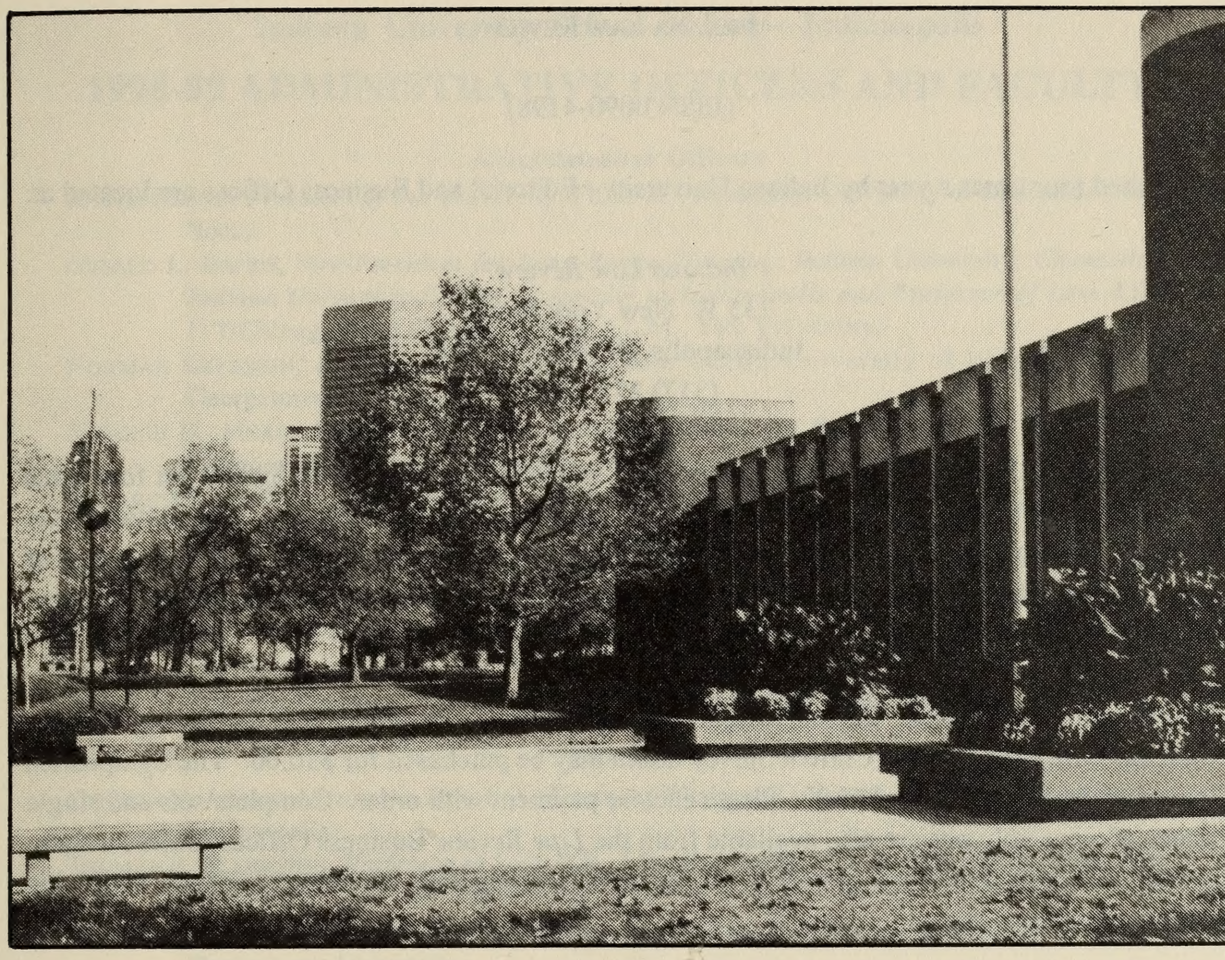

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SURVEY

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MOVING THE ROCK: THE CONSTANT NEED TO RE-INVENT THE PROFESSION USING THE NATION'S JUDICIARY AS LEADERS

RANDALL T. SHEPARD*

As renewed calls for legal reform reverberate across the country and the legal profession and its customers wrestle with how our profession will function in the new century, I am struck by the image of Sisyphus toiling ceaselessly to roll his rock up the hill, only to begin once again, and again.

Those in our profession who argue earnestly for reform must often feel like the figure of Greek myth. Efforts at reform are frequently hard to begin, sometimes difficult to implement, and often impossible to sustain.

This is not to say there have not been successes and victories, but calls for change persist. The task of moving the rock of reform up the hill never quite seems to be over. We are the brothers and sisters of Sisyphus.

That by itself is not reason for despair. The redesign of human institutions is the way societies evolve, and it is almost always worth the effort. Even modest improvements are usually worth the investment, as frustrating as the pace of the progress may be.

Certainly, it is far more satisfying to effect broad and lasting changes. To make improvements more enduring, we must make full use of all the resources that might be brought to bear. I write here to suggest greater use of a valuable, but often overlooked resource: the nation's judges.

The women and men who make up our country's bench must be central figures in any real, sustainable effort to improve our legal system. In my view, a three-level effort is required. First, we should encourage them to participate in innovative efforts at reform even if their ideas rattle traditional notions of what a judge should do and be. Second, we must make sure a key part of their task is to involve the public stakeholders in the process. Finally, we must enroll judges in institutionalizing efforts at reexamination and reform while still keeping those efforts fresh and invigorating.

I. DEFINING THE PRESENT PROBLEMS

Reformers worth their salt are always on the lookout for handy dragons to slay. Public discontent with the legal system has long been such a reptile. The frequency with which such reformers point to popular dissatisfaction may tend to dull insiders to the reality that there is hard data that supports the existence of this particular dragon.

Our friends at the American Bar Association (the "ABA") waded into the rivers of discontent by asking the people what they thought about law firms. Their 1993 survey showed, for example, that public confidence in law firms had declined substantially since the 1970s.[1] A poll taken in the mid-1970s, when

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* Chief Justice of Indiana. A.B., 1969, Princeton University; J.D., 1972, Yale Law School; LL.M., 1995, University of Virginia School of Law.

1. Gary A. Hengstler, *Vox Populi, The Public Perception of Lawyers: ABA Poll*, A.B.A.

turmoil linked to the Vietnam War was fresh in the public mind, found that 25% of Americans believed lawyers had high or very high ethical standards. By 1993, Americans who believed attorneys had high ethical standards had dipped to just 16%.[2]

A 1996 study in Florida using telephone surveys and focus groups asked the telephone respondents to identify five problems with the courts and then asked the focus group participants to prioritize them. The problems identified, in order of priority, were: 1) courts are too lenient with criminals; 2) courts do not treat everyone the same; 3) courts take too long; 4) courts are too complicated; and 5) information on the courts is too hard to obtain.[3]

The telephone survey found that 42.3% of respondents replied negatively when asked: "What is the first thing that comes to mind when thinking about the Florida State Courts system?"[4] If we can take any solace in these replies (and we should not take much), it is in the fact that the Florida court system ranked above the federal courts, the Florida legislature, the governor's office, the news media and the public schools when respondents were asked if they had some level of confidence in various public institutions. Only the local police and local county government scored higher.[5]

While it is unclear whether these trends are linked to dissatisfaction with the judicial system in general or lawyers in particular, there are reasons to expect that the public's negative reactions to its encounters with the system will not just vanish. For example, an up tick in the number of pro se litigants has been spotted.[6] Few state or federal court systems feature any kind of organized aid for people who try to solve simple legal problems on their own.[7] While the responses to pro se litigation are controversial, doing nothing is likely to only increase frustration and dissatisfaction among the public. Surely, it will not produce more justice.

Even for those who toil within the system, feelings of dissatisfaction run deep. There is a strong sense that race and gender bias persist. The *ABA Journal* recognized this in a 1999 multi-part story detailing problems with prejudice. In tandem with the *National Bar Association Magazine*, the *ABA Journal* commissioned a poll of black and white lawyers. The results warrant serious consideration. "More than half of black lawyers in the survey . . . , when asked how much racial bias exists in the justice system, answered 'very much.' Nearly

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J., Sept. 1993, at 60, 63-64.

2. Randall T. Shepard, *Lawyer-Bashing and the Challenge of a Sensible Response*, 27 IND. L. REV. 699, 700 (citing Randall Samborn, *Tracking Trends*, NAT'L L.J., Aug. 9, 1993, at 20).

3. JAY RAYBURN, JUDICIAL MANAGEMENT COUNCIL, REPORT OF FOCUS GROUP RESEARCH 3a (1996) (copy on file with the *Indiana Law Review*).

4. COMMITTEE ON COMMUNICATION & PUBLIC INFORMATION, JUDICIAL MANAGEMENT COUNCIL, FLORIDA STATEWIDE PUBLIC OPINION SURVEY, EXECUTIVE SUMMARY 2 (1996) (copy on file with the *Indiana Law Review*).

5. *See id.* at 9.

6. *See* John Gibeaut, *Turning Pro Se*, A.B.A. J., Jan. 1999, at 28.

7. *See id.*

a third of the white lawyers answered 'very little,' although more than half said there is 'some.'"[8]

If there is this much concern among inside players in the justice system, just imagine how the "customers" feel.

Many problems of this sort have a familiar ring to them. While we lawyers bristle at outside criticisms, we complain to others about the system's problems and frequently agree about what they are. In an article in 1994, I noted that:

> Americans tell us they believe that the judicial process is too slow, too expensive, and too complicated, and we must be more than ready to accept their judgment. Only by seeing ourselves through the public's eyes and taking their criticisms seriously can we alleviate their frustration, improve the legal system and repair our professional image.[9]

Our task is complicated by the seemingly schizophrenic way some members of the public look at our profession. It is reminiscent of the public opinion polls suggesting that citizens hold Congress as an institution in contempt, but like their own member of Congress just fine. As a pair of observers have noted: "The lay attitude towards lawyers is a compound of contradictions, a mingling of respect and derision. Although lawyers occupy leading positions in government and industry, although the public looks to them for guidance in meeting its vital problems, concurrently it sneers at them as tricksters and quibblers."[10]

Notwithstanding this level of mistrust, we must focus our energy on the causes of discontent instead of the perceptions.[11] There is much at stake, and not just for those of us who draw our bread from this system. As Frances Zemans has observed: "The public will not benefit in the long run if public confidence in the courts continues to decline, as evidence indicates that it is."[12] In their articles suggesting that disclosure of disciplinary sanctions levied against attorneys be included in all legal advertising, Sandra L. DeGraw and Bruce W. Burton put it even more bluntly: "[T]here exists a public policy question concerning the continued effectiveness of the administration of justice in a climate of growing mistrust and hostility toward legal institutions generally and lawyers specifically."[13] It is far from an easy task.

II. WHY USE JUDGES TO EFFECT CHANGE

Some might question using judges to reform a system in which they are so

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8. Terry Carter, *Divided Justice*, A.B.A. J., Feb. 1999, at 43.

9. Shepard, *supra* note 2, at 699.

10. Sonia Sotomayor & Nicole A. Gordon, *Returning Majesty to the Law and Politics: A Modern Approach*, 30 SUFFOLK U. L. REV. 35, 36 (1996).

11. *See* Shepard, *supra*, note 2, at 699.

12. Frances Kahn Zemans, *From Chambers to Community*, JUDICATURE, Sept.-Oct. 1996, at 62, 63.

13. Sandra L. DeGraw & Bruce W. Burton, *Lawyer Discipline and "Disclosure Advertising": Towards A New Ethos*, 72 N.C. L. REV. 351, 367-68 (1994).

inextricably involved. I say, how can one succeed without using them? Our nation's trial and appellate judges work daily at the intersection of all the fault lines of a society in the midst of sweeping change—a society that seeks redress and resolution from the court system.

Whether most judges are well-suited to such leadership is a harder question. Many judges are appointed through merit selection and do not acquire the political skills learned in the hurly-burly of a campaign. Others are limited in the ways in which they can conduct their judicial election campaigns. Judges who face retention votes must deal with similar strictures. While this means that some judges are more able reformers than others, as a class they are hardly aloof or unconcerned about the people for whom they labor. Few judges forget the source of their authority. The drafters of some of our most seminal literature knew this long ago. "As early as our nation's founding, the *Federalist Papers* referred to the courts as having neither the power of the purse nor the power of the sword. That means the judiciary relies upon a voluntary grant of authority by the public."[14]

As elected or appointed officials, judges at the trial and appellate level are natural recruits for any effort at reform. To be sure, there is risk of criticism in any decision to step outside classic roles. They will need some help. "If judges are to feel comfortable with a leadership role in promoting public understanding of the courts, a balance must be reached between that role and the need to maintain the appearance and reality of impartiality."[15] A judicial education curriculum developed by the American Judicature Society last year may give judges the means to find that balance.

We are hardly at a loss for examples of judges playing an important role without running into case conflicts or professional barriers. Former Florida Chief Justice Arthur England is widely regarded as the founder of the Interest on Lawyer Trust Accounts ("IOLTA") movement. Judge Judith Billings has been a national leader in the effort to involve judges in pro bono programs. The late Arthur Vanderbilt prompted change across a whole spectrum of topics.

In Indiana, our supreme court appointed fourteen trial judges to lead pro bono efforts across the state under our Voluntary Attorney Pro Bono Plan.[16] The court's decision to select trial judges as the leaders of these efforts was not an accident. An early appointee, Judge David Dreyer of the Marion Superior Court has been able to use the platform of his office to convene meetings attended by representatives from all the pro bono organizations in Central Indiana as well as nearly every bar association from the counties around Indianapolis.[17]

We have had many other instances where Indiana judges have devised creative ways to reach out and into the community. In addition to the normal range of Law Day activities, judges have run "Saturday School" sessions to

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14. Zemans, *supra* note 12, at 62.

15. Editorial, *Helping Judges Explain the Courts*, JUDICATURE, Sept.-Oct. 1996, at 56.

16. IND. RULES OF PROFESSIONAL CONDUCT Rule 6.5 (1999).

17. *See* Cary Solida, *Pro Bono Councils, Commission Moving Forward*, IND. LAW., Oct. 28-Nov. 10, 1998, at 5.

improve the study habits of juvenile delinquents. Others have held a "Parent University" to assist parents in improving decision-making skills. The Noble County bench has sponsored one-day seminars with national speakers that are designed to help the local legal community serve its clients better.[18]

Many have viewed these "out from behind the bench" efforts as vital to the continued strength of the judiciary for, "[i]f judges are truly committed to the rule of law and an independent judiciary, it is their obligation to reach out to the public about these important concepts. If judges do not reach out, no one else is going to do it for them."[19] Although the news media and bar associations can assist a judge's outreach effort, those organizations really won't do any educating from the judge's point of view.[20]

For both judges and lawyers, efforts toward improvement must be systematic. While projects dealing with public perception have their place, it is vital that any reform efforts go right to the root of our problems. The ABA made a concerted effort in the early 1990s to address the public image of attorneys. This particular effort focused on correcting the perceptions, but it was short on addressing the cause of problems within the justice system.[21] Subsequent ABA initiatives have been more focused on substantive matters.[22] The National Summit on Public Trust and Confidence, devised by the Conference of Chief Justices and the ABA has been the most sophisticated effort yet.

Taking concrete steps to reform the discovery process and reduce expensive and unnecessary requests (that are too often tactics used more to wear the opponent down than bids to elicit the facts) is one step that would improve the system itself by making it less costly and confrontational. Encouraging pre-suit mediation and alternative dispute resolution will help convince the public that their disputes will not get lost in a judicial black hole.[23] Opening up the lawyer discipline process, as we have done in Indiana, will instill public confidence because it will help convince the public that we are serious about dealing with professional misconduct.

Professional discipline is a continuing sore spot with clients, though it has had some attention of late. The trend toward more openness in disciplinary systems may help the public make better choices about the lawyers they hire and counter the often haphazard dissemination of information about attorney and judicial discipline. But a new Indiana Admission and Discipline Rule does explicitly require attorneys to tell their existing clients of their disbarment. The

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18. *See* Randall T. Shepard, Indiana Courts as Servants of Their Communities, Address before the Indiana General Assembly (Jan. 14, 1998) (transcript available from the Indiana Supreme Court).

19. Zemans, *supra* note 12, at 62.

20. *See id.*

21. *See* Shepard, *supra* note 2, at 701.

22. An example of this was the ABA Just Solutions Project. Despite tremendous legwork for it and enthusiasm about it, the project nearly faced extinction before it was even born. In the end, the ABA Just Solutions Project was funded, but just barely. *See* Shepard, *supra* note 2, at 708.

23. *See id.* at 705-07.

rules also require attorneys suspended from the practice of law to notify clients of the nature and duration of their suspension.[24]

In an article that advocated taking aggressive steps to regulate the profession while also speaking up when the legal system is unjustly criticized, two authors note that "[t]he response that can give the public confidence in our profession is our own leadership in weeding out the fraudulent and wrongful conduct that the public rightly condemns . . . ."[25]

Other authorities have suggested that we go further than "simply" work to eradicate misconduct. It might even be useful if we address those problems that do not rise to the level of misconduct but which are annoying or uncivil.

> If we can persuade the public that the system we have in place and the roles played by lawyers within that system are the best available, there remain ancillary issues of an ethical nature that do not necessarily involve what happens in the courtroom. We have an obligation, for example, to address professional conduct perceived by the public to be wrong even if it is not necessarily illegal.[26]

Whether it is advocating for openness in the discipline process, helping set up pro bono projects or helping troubled teens through school, judges can be leaders in these efforts with a minimal risk of conflict.

III. Involving the Public

Ultimately, any effort at changing the judicial system must involve the people who are served by it. Indiana has taken several steps to involve the public in our processes.

There is now a thirty-year tradition of participation by non-lawyers in the most important institutions of the profession. Since 1970, three members of the seven-member Indiana Judicial Nominating Commission, which regulates the conduct of judges and recruits applicants for the appellate courts, must by law be non-lawyers.[27] More recently, the Indiana Supreme Court has decided that the nine-member Disciplinary Commission, which handles issues of lawyer conduct, must have two non-lawyer members.[28] The membership of the local groups organizing pro bono efforts under our Voluntary Attorney Pro Bono Plan must include two members from the "community-at-large."[29] A group created by the Indiana Judges Association and the Indiana State Bar Association, the Indiana Citizens Commission for the Future of Indiana Courts, is working toward jury system improvement and increasing the public's access to justice. Its membership includes business leaders, educators, community group leaders, and

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24. Ind. Admis. & Disc. Rs. 23(26)(a) & (c) (1999).
25. Sotomayor & Gordon, *supra* note 10, at 46.
26. *Id.* at 47.
27. Ind. Code § 33-2.1-4-1(a) (1998).
28. *See* Ind. Admis. & Disc. R. 23(6)(b) (1999).
29. Ind. Rules of Professional Conduct Rule 6.5(f)(1)(C) (1999).

officials from all three branches of government—collectively a sweeping representation of the population. The Indiana Public Trust working group that prepared for the May 1999 Public Trust and Confidence effort also included non-lawyer members of the public.

Although our work in this area is not yet done, I think we have embraced the spirit enunciated by ABA President Philip S. Anderson when he wrote about the importance of involving the public in new efforts to improve the system:

> Justice initiatives make the public part of a consultative process through various methods such as citizen conferences, commissions on the future of the courts, and citizen summits. The process produces fresh ideas about how the justice system can be improved . . . . It builds public confidence in the system by demonstrating to the public that judges and lawyers are listening and are willing to respond to public concerns.[30]

It is vital to partner with non-legal groups and begin to see so-called "court watcher" groups as partners in the process of progress instead of as a freelance chorus of critics. "What we should also acknowledge, to broaden the true reach of the law's majesty, is the role that many influences, including the press and lay public, play in contributing to our intricate legal system."[31]

We should also make every effort to involve the members of the Fourth Estate. This will not be an easy task either. In some quarters of the bench and bar mistrust for the media runs quite high. For the judiciary, some of this bad blood begins at the highest court in the land. Legend has it that the U.S. Supreme Court has what has come to be known as the "90-second rule." According to court lore, any law clerk seen talking to a reporter for more than ninety seconds is summarily fired.[32] That this implausible proposition is even a part of internal folk lore is instructive.

In Indiana, the press and bench are working on several joint projects. A group of journalists and judges have been sharing box lunches in informal meetings for about a year now to discuss various issues of common concern. Another group is planning a one-day "Law School for Journalists" that is set for June 1999.[33] Both initiatives may serve each others' interest by getting a better feel for how each side operates.

As I think about each of these Indiana initiatives, I am struck by the extent to which judges have helped make them all happen. Our partners in the bar have been there carrying a large share of the load at virtually every juncture, but judges have a special capacity to build bridges to other parts of the society. We need to use this capacity whenever we can.

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30. Philip S. Anderson, *Incremental Steps Toward Justice*, A.B.A. J., Jan. 1999, at 8.

31. Sotomayor & Gordon, *supra* note 10, at 50.

32. *See* Steve France, *A Penchant For Privacy*, A.B.A. J., Dec. 1998, at 38.

33. *See* Scott Olson, *Journalists Will Have the Opportunity to Attend Law School*, IND. LAW., Dec. 23, 1998-Jan. 5, 1999, at 5.

IV. Making Improvements Last: Letting Sisyphus Rest

Even the most earnest of reformers occasionally feel frustrated at times about the slow pace of improvements, or the lack of change. At times, clarion calls for "blue ribbon committees" and "white papers" and "visioning exercises" sometimes seem too commonplace and ring a little hollow.

Fears that any new exercise will simply create a ponderous document stuffed with well-meaning phrases that will disappear onto a dusty shelf or the dark corner of a hard drive must spring up any time a new commission, committee or group is formed to examine change in the legal system. Planners of an upcoming ABA conference on racial and ethnic justice are working to avoid this kind of a result. Last fall, Beverly McQueary-Smith, president of the National Bar Association noted: "We don't want to come up with just another nice, glossy, shiny report. This group wants an action plan."[34]

My guess is that many well-meaning people must have felt that way when details of the 1999 National Conference on Trust and Confidence in the Justice System were first revealed. Sponsored by the Conference of Chief Justices, the ABA, the League of Women Voters and the Conference of State Court Administrators, this May 1999 gathering in Washington plainly will be a cut above the usual. ABA President Philip Anderson, in describing the ABA's aspirations for the meeting explained: "This program will bring together the chief justices, state and federal judges, lawyers and the public to devise a national strategy to strengthen and reinforce public understanding and support of the principle that an independent judiciary is essential to a free society."[35]

My view is that the Public Trust and Confidence Project will have some staying power. An array of very influential groups is behind it. Each state was asked to send a five-person team. Indiana's effort has been led by Indiana Court of Appeals Judge James S. Kirsch. His group worked through most of 1998 to identify what is eroding the public's trust and confidence in the justice system. The Indiana group then devised a set of concrete steps and strategies the courts can take to restore that trust. National organizers of the conference used those issues and strategies to plan the conference and select the presenters. The people who gather in Washington will develop strategies that can be institutionalized in ways that will produce on-going, enduring change.

If we do not work to preserve the public's trust, the future for all of us in this profession may be quite dire. "[I]f the bench and bar of America are unable to shore up their eroding claims to public trust confidence, then the institution that has become most vital to the functioning of a society based on law is called into question. Loss of public trust and confidence eventually could prove to be socially seismic."[36]

Now is the time to put our shoulder to rock alongside Sisyphus and keep pushing onward, no matter how long it takes.

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34. James Podgers, *More Than Just Talk*, A.B.A. J., Nov. 1998, at 92.

35. Anderson, *supra* note 30, at 8.

36. DeGraw & Burton, *supra* note 13, at 369.

AN EXAMINATION OF THE INDIANA SUPREME COURT DOCKET, DISPOSITIONS, AND VOTING IN 1998*

KEVIN W. BETZ**
MARK A. LINDSEY***

In 1998, the Indiana Supreme Court's docket, dispositions, and voting were again overwhelmed by its mandatory criminal appeals—the highest percentage in the eight years of this study. Because of this crush of mandatory appeals, the court also issued its lowest number of discretionary civil appeals.[1]

Faced with this type of docket, the court's members have also decreased their productivity and have the highest percent of unanimous opinions in the period of this study. Fortunately, the court is nearing a constitutional change in its mandatory jurisdiction. Pursuant to the Indiana Constitution, the Indiana General Assembly must pass this change for the second time in this year's session and then it will be placed on the state-wide ballot.[2]

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* The tables presented in this Article are patterned after the annual statistics of the U.S. Supreme Court published in the *Harvard Law Review*. An explanation of the origin of these tables can be found at Louis Henkin, *The Supreme Court, 1967 Term*, 82 HARV. L. REV. 63, 301 (1968). The *Harvard Law Review* granted permission for the use of these tables by the *Indiana Law Review* this year; however, permission for any further reproduction of these tables must be obtained from the *Harvard Law Review*.

We thank Barnes & Thornburg for its gracious willingness to devote the time, energy, and resources of its law firm to allow a project such as this to be accomplished. As is appropriate, credit for the idea for this project goes to Chief Justice Shepard; but, of course, any errors or omissions belong to his former law clerk. We also thank WESTLAW® for its kind willingness to allow us free access to its computer resources and assistance in preparing these tables.

** Attorney at Law, representing employees and professionals and practicing in the appellate area, 1997-present. Former Chief Counsel and Deputy Commissioner, Indiana Department of Environmental Management, 1995-97. Associate, Krieg DeVault Alexander & Capehart, Indianapolis, 1990-95. Law clerk for Chief Justice Randall T. Shepard, Indiana Supreme Court, 1988-90. B.A., 1982, Indiana University; M.S., 1984, Northwestern University; J.D., 1988, Indiana University School of Law—Bloomington.

*** Associate, Barnes & Thornburg, 1996-present; B.A., 1993, Indiana University; J.D., 1996, Indiana University School of Law—Indianapolis.

1.

	MANDATORY	DISCRETIONARY	TOTAL
1991	109 (53%)	98 (47%)	207
1992	64 (41%)	93 (59%)	157
1993	60 (44%)	77 (56%)	137
1994	60 (45%)	73 (55%)	133
1995	46 (38%)	76 (62%)	122
1996	68 (59%)	48 (41%)	116
1997	100 (58%)	71(42%)	171
1998	84 (63%)	50 (37%)	134

2. The court fought this battle against an overwhelming number of mandatory criminal cases in 1988. The court is fighting the battle again. *See* Kevin W. Betz & Andrew T. Deibert, *An Examination of the Indiana Supreme Court Docket, Dispositions, and Voting in 1996*, 30 IND. L. REV. 933 (1997); *see also* Randall T. Shepard, *Changing the Constitutional Jurisdiction of the*

The following is a description of the highlights from each table.

Table A. In 1998, the supreme court issued 141 opinions that were authored by an individual justice. This is a decrease from last year's 171 opinions authored by an individual justice. Of the 141 opinions issued in 1998, only 35 were civil opinions and 106 were criminal. This is the fewest number of civil opinions since 1990.

The court as a whole issued 40 per curiam opinions—38 civil and 2 criminal. Almost all 38 civil opinions were attorney discipline matters.

The only individual justice that did not decrease in productivity was Justice Boehm who issued the same number of opinions as last year—43. He issued 25 criminal opinions, which was roughly even with the other justices' output of criminal opinions; but he also rendered 18 civil opinions, which is more than triple the number of civil opinions issued by any other justice.

Chief Justice Shepard was next with 30 opinions; Justice Sullivan issued 29; Justice Dickson authored 20; and Justice Selby wrote 19.

The court also issued the fewest number of dissents in the 8 years of this study—23. Justice Sullivan, as in the past, had the most dissents with 9. Justice Dickson, as in the past also, was next with 7.

Table B-1. For civil cases, Justices Selby and Shepard were the two justices most aligned at 97.2%. Justices Selby and Boehm were next at 94.1%. As in the past, Justices Shepard and Sullivan were the least aligned at 84.4%.

Justice Selby was the most aligned with other justices, and Justice Sullivan was the least aligned overall.

Table B-2. For criminal cases, Justices Shepard and Boehm were the most aligned at 96.3%, which is the same as last year. Justices Sullivan and Dickson were the least aligned at 89.8%, which is also the same as last year. As for criminal cases overall, Justice Shepard was the most aligned with his fellow justices.

Table B-3. For all cases, Chief Justice Shepard and Justice Boehm, and Chief Justice Shepard and Justice Selby, are the most aligned pairs of justices—each pair in agreement 95.1% of the time. This is nearly identical to last year's results. The two least aligned justices, also the same as last year, were Justices Sullivan and Dickson at 89.3%.

Overall, Chief Justice Shepard was the most aligned with his fellow justices.

Table C. As seen last year, the court's unanimity increased because of the less-divisive mandatory docket of cases. In 1998, the court was either unanimous or unanimous with concurrence in 88% of its opinions. This is equal to last year's

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Indiana Supreme Court: Letting a Court of Last Resort Act Like One, 63 IND. L.J. 669 (1988); Randall T. Shepard, *Foreword: Indiana Law, the Supreme Court, and a New Decade*, 24 IND. L. REV. 499 (1991).

percentage, which is the highest in the eight years of this study.

Table D. The court issued only 3 split decisions that were composed of only a three-justice majority. This is by far the lowest number of such split opinions in the history of this study—if not in the history of the court. Last year was the next lowest number of 3-2 opinions with 6 such decisions. Chief Justice Shepard was the author of 2 of the 3 split opinions.

Table E-1. The court affirmed almost 90% of the mandatory criminal appeals, which was also the majority of its docket. This is compelling evidence in support of a move to change the court's jurisdiction. Obviously, if the jurisdiction were changed, the court would not even have decided the vast majority of these appeals.

Table E-2. The court decreased the number of civil petitions it transferred from 45 in 1997 to 32 in 1998. Interestingly, in 1997 there were no petitions to transfer in juvenile cases, but in 1998 there were a total of 24 and 3 were granted.

A civil petition to transfer stood about a 10% chance of being granted, and a criminal petition stood about a 6% chance of being granted.

Table F. The court continues to demonstrate its interest in the Indiana Constitution with 14 opinions involving such issues, although this, too, is a drop from last year where there were 24 such cases. There were also only 9 death penalty cases reviewed, which is on par with recent years except last year when the court reviewed 18 death penalty cases. The court reversed only 1 of those 9 death penalty cases.

TABLE A
OPINIONS[a]

	OPINIONS OF COURT[b]			CONCURRENCES[c]			DISSENTS[d]		
	Criminal	Civil	Total	Criminal	Civil	Total	Criminal	Civil	Total
Shepard, C.J.	22	8	30	1	0	1	0	1	1
Dickson, J.	17	3	20	1	1	2	3	4	7
Sullivan, J.[e]	24	5	29	1	1	2	6	3	9
Selby, J	18	1	19	3	0	3	2	0	2
Boehm, J.[e]	25	18	43	1	0	1	2	2	4
Per Curiam	2	38	40						
Total	108	73	181	7	2	9	13	10	23

[a] These are opinions and votes on opinions by each justice and in per curiam in the 1998 term. The Indiana Supreme Court is unique because it is the only supreme court to assign each case to a justice by a consensus method. Cases are distributed by a consensus of the justices in the majority on each case either by volunteering or nominating writers. The Chief Justice does not have any power to control the assignments other than as a member of the majority. *See* Melinda Gann Hall, *Opinion Assignment Procedures and Conference Practices in State Supreme Courts*, 73 JUDICATURE 209 (1990). The order of discussion and voting is started by the most junior member of the court and follows reverse seniority. *See id.* at 210.

[b] This is only a counting of full opinions written by each justice. Plurality opinions that announce the judgment of the court are counted as opinions of the court. It includes opinions on civil, criminal, and original actions. Also, the following 7 miscellaneous cases are not included in the table: Winkler v. Winkler, 699 N.E.2d 657 (Ind. 1998) (dissent from denial of transfer); Davenport v. State, 696 N.E.2d 870 (Ind. 1998) (denial of petition to reinstate convictions); Pruitt v. City of Lake Station, 695 N.E.2d 123 (Ind. 1998) (order dismissing appeal as moot); Town of St. John v. State Bd. of Tax Comm'rs, 695 N.E.2d 123 (Ind. 1998) (order granting petitions for review and setting oral argument); Worldcom Network Servs., Inc. v. Thompson, 694 N.E.2d 1125 (Ind. 1998) (order denying petition to hold appellee in contempt); Indiana High Sch. Athletic Ass'n v. Carlberg, 694 N.E.2d 222 (Ind. 1998) (dissent from denial of rehearing); National City Bank, Ind. v. Shortridge, 691 N.E.2d 1210 (Ind. 1998) (denial of motion for retroactive disqualification of supreme court justice).

[c] This category includes both written concurrences and votes to concur in result only.

[d] This category includes both written dissents and votes to dissent without opinion. Opinions concurring in part and dissenting in part or opinions concurring in part only and differing on another issue are counted as dissents.

[e] Justices declined to participate in the following non-disciplinary cases: Shell Oil Co. v. Meyer, 705 N.E.2d 962 (Ind. 1998); Shell Oil Co. v. Lovold Co., 705 N.E.2d 981 (Ind. 1998); Walker v. State, 694 N.E.2d 258 (Ind. 1998) (Justice Sullivan); McClain v. Review Bd. of the Ind. Dep't of Workforce Dev., 693 N.E.2d 1314 (Ind. 1998); Melrose v. Capitol City Motor Lodge, Inc., 705 N.E.2d 985 (Ind. 1998); State Bd. of Tax Comm'rs v. Town of St. John, 702 N.E.2d 1034 (Ind. 1998) (Justice Boehm).

TABLE B-1
VOTING ALIGNMENTS FOR CIVIL CASES[f]
NOT INCLUDING JUDICIAL OR ATTORNEY DISCIPLINE CASES

		Shepard	Dickson	Sullivan	Selby	Boehm
Shepard, C.J.	O	---	33	27	35	31
	S		0	0	0	0
	D		33	27	35	31
	N		36	32	36	34
	P		91.7%	84.4%	97.2%	91.2%
Dickson, J.	O	33	---	27	34	30
	S	0		1	0	0
	D	33		28	34	30
	N	36		32	36	34
	P	91.7%		87.5%	94.4%	88.2%
Sullivan, J.	O	27	27	---	28	26
	S	0	1		0	1
	D	27	28		28	27
	N	32	32		32	30
	P	84.4%	87.5%		87.5%	90.0%
Selby, J.	O	35	34	28	---	32
	S	0	0	0		0
	D	35	34	28		32
	N	36	36	32		34
	P	97.2%	94.4%	87.5%		94.1%
Boehm, J.	O	31	30	26	32	----
	S	0	0	1	0	
	D	31	30	27	32	
	N	34	34	30	34	
	P	91.2%	88.2%	90.0%	94.1%	

[f] This table records the number of times that one justice voted with another in full-opinion decisions, including per curiam, for civil cases only. For example, in the top set of numbers for Chief Justice Shepard, 33 is the number of times Chief Justice Shepard and Justice Dickson agreed in a full majority opinion in a civil case. Two justices are considered to have agreed whenever they joined the same opinion, as indicated by either the reporter or the explicit statement of a justice in the body of his or her own opinion. The table does not treat two justices as having agreed if they did not join the same opinion, even if they agreed only in the result of the case or wrote separate opinions revealing little philosophical disagreement.

"O" represents the number of decisions in which the two justices agreed in opinions of the court or opinions announcing the judgment of the court.

"S" represents the number of decisions in which the two justices agreed in separate opinions, including agreements in both concurrences and dissents.

"D" represents the number of decisions in which the two justices agreed in either a majority, dissenting, or concurring opinion.

"N" represents the number of decisions in which both justices participated and thus the number of opportunities for agreement.

"P" represents the percentage of decisions in which one justice agreed with another justice, calculated by dividing "D" by "N."

TABLE B-2
VOTING ALIGNMENTS FOR CRIMINAL CASES NOT INCLUDING JUDICIAL OR ATTORNEY DISCIPLINE CASES[g]

		Shepard	Dickson	Sullivan	Selby	Boehm
Shepard, C.J.	O		103	101	102	104
	S		0	0	0	0
	D	---	103	101	102	104
	N		108	108	108	108
	P		95.4%	93.5%	94.4%	96.3%
Dickson, J.	O	103		97	99	101
	S	0		0	0	0
	D	103	---	97	99	101
	N	108		108	108	108
	P	95.4%		89.8%	91.7%	93.5%
Sullivan, J.	O	101	97		97	99
	S	0	0		1	1
	D	101	97	---	98	100
	N	108	108		108	108
	P	93.5%	89.8%		90.7%	92.6%
Selby, J.	O	102	99	97		100
	S	0	0	1		0
	D	102	99	98	---	100
	N	108	108	108		108
	P	94.4%	91.7%	90.7%		92.6%
Boehm, J.	O	104	101	99	100	
	S	0	0	1	0	
	D	104	101	100	100	---
	N	108	108	108	108	
	P	96.3%	93.5%	92.6%	92.6%	

[g] This table records the number of times that one justice voted with another in full-opinion decisions, including per curiam, for criminal cases only. For example, in the top set of numbers for Chief Justice Shepard, 103 is the number of times Chief Justice Shepard and Justice Dickson agreed in a full majority opinion in a criminal case. Two justices are considered to have agreed whenever they joined the same opinion, as indicated by either the reporter or the explicit statement of a justice in the body of his or her own opinion. The table does not treat two justices as having agreed if they did not join the same opinion, even if they agreed only in the result of the case or wrote separate opinions revealing little philosophical disagreement.

"O" represents the number of decisions in which the two justices agreed in opinions of the court or opinions announcing the judgment of the court.

"S" represents the number of decisions in which the two justices agreed in separate opinions, including agreements in both concurrences and dissents.

"D" represents the number of decisions in which the two justices agreed in either a majority, dissenting, or concurring opinion.

"N" represents the number of decisions in which both justices participated and thus the number of opportunities for agreement.

"P" represents the percentage of decisions in which one justice agreed with another justice, calculated by dividing "D" by "N."

TABLE B-3
VOTING ALIGNMENTS FOR ALL CASES NOT INCLUDING JUDICIAL OR ATTORNEY DISCIPLINE CASES[h]

		Shepard	Dickson	Sullivan	Selby	Boehm
Shepard, C.J.	O	---	136	128	137	135
	S		0	0	0	0
	D		136	128	137	135
	N		144	149	144	142
	P		94.4%	91.4%	95.1%	95.1%
Dickson, J.	O	136	---	124	133	131
	S	0		1	0	0
	D	136		125	133	131
	N	144		140	144	142
	P	94.4%		89.3%	92.4%	92.3%
Sullivan, J.	O	128	124	---	125	125
	S	0	1		1	2
	D	128	125		126	127
	N	140	140		140	138
	P	91.4%	89.3%		90.0%	92.0%
Selby, J.	O	137	133	125	---	132
	S	0	0	1		0
	D	137	133	126		132
	N	144	144	140		142
	P	95.1%	92.4%	90.0%		93.0%
Boehm, J.	O	135	131	125	132	---
	S	0	0	2	0	
	D	135	131	127	132	
	N	142	142	138	142	
	P	95.1%	92.3%	92.0%	93.0%	

[h] This table records the number of times that one justice voted with another in full-opinion decisions, including per curiam, for all cases. For example, in the top set of numbers for Chief Justice Shepard, 136 is the total number of times Chief Justice Shepard and Justice Dickson agreed in all full majority opinions written by the court in 1998. Two justices are considered to have agreed whenever they joined the same opinion, as indicated by either the reporter or the explicit statement of a justice in the body of his or her own opinion. The table does not treat two justices as having agreed if they did not join the same opinion, even if they agreed only in the result of the case or wrote separate opinions revealing little philosophical disagreement.

"O" represents the number of decisions in which the two justices agreed in opinions of the court or opinions announcing the judgment of the court.

"S" represents the number of decisions in which the two justices agreed in separate opinions, including agreements in both concurrences and dissents.

"D" represents the number of decisions in which the two justices agreed in either a majority, dissenting, or concurring opinion.

"N" represents the number of decisions in which both justices participated and thus the number of opportunities for agreement.

"P" represents the percentage of decisions in which one justice agreed with another justice, calculated by dividing "D" by "N."

TABLE C

UNANIMITY
NOT INCLUDING JUDICIAL OR ATTORNEY DISCIPLINE CASES[i]

Unanimous[j]			Unanimous With Concurrence[k]			Opinions With Dissent			Total
Criminal	Civil	Total	Criminal	Civil	Total	Criminal	Civil	Total	
91	29	120(83.3%)	6	1	7(4.9%)	11	6	17(11.8%)	144

[i] This table tracks the number and percent of unanimous opinions among all opinions written. If, for example, only four justices participate and all concur, it is still considered unanimous. It also tracks the percent of overall opinions with concurrence and overall opinions with dissent.

[j] A decision is considered unanimous only when all justices participating in the case voted to concur in the court's opinion as well as its judgment. When one or more justices concurred in the result, but not in the opinion, the case is not considered unanimous.

[k] A decision is listed in this column if one or more justices concurred in the result, but not in the opinion of the court or wrote a concurrence and there were no dissents.

TABLE D

3-2 DECISIONS[l]

Justices Constituting the Majority	Number of Opinions[m]
1. Shepard, C.J., Dickson, J., Boehm, J.	1
2. Shepard, C.J., Dickson, J., Selby, J.	2
Total[n]	3

[l] This table reflects only decisions rendered by full opinion. An opinion is counted as a 3-2 decision if two justices voted to decide the case in a manner different from that of the majority of the court.

[m] This column lists the number of times each three-justice group constituted the majority in a 3-2 decision.

[n] The 1998 term's 3-2 decisions were:

1. Shepard, C. J., Dickson, J., Boehm, J.: Garner v. State, 704 N.E.2d 1011 (Ind. 1998) (Shepard, C.J.).

2. Shepard, C.J., Dickson, J., Selby, J.: Meridian Mut. Ins. Co. v. Auto-Owners Ins. Co., 698 N.E.2d 770 (Ind. 1998) (Shepard, C.J.); Jackson v. State, 697 N.E.2d 53 (Ind. 1998) (Dickson, J.).

TABLE E-1

DISPOSITION OF CASES REVIEWED BY TRANSFER AND DIRECT APPEALS[o]

	Reversed or Vacated[p]	Affirmed	Total
Civil Appeals Accepted for Transfer	26 (78.8%)	7 (21.2%)	33
Direct Civil Appeals	0	0	0
Criminal Appeals Accepted for Transfer	9 (52.9%)	8 (47.1%)	17
Direct Criminal Appeals	11 (13.1%)	73 (86.9%)	84
Total	46 (34.3%)	88 (65.7%)	134[q]

[o] Direct criminal appeals are cases in which the trial court imposed a sentence of greater than 50 years. *See* IND. CONST. art. VII, § 4. Thus, direct criminal appeals are those directly from the trial court. A civil appeal may also be direct from the trial court. *See* IND. R. APP. P. 4(A); *see also* IND. ORIG. ACT. RS. All other Indiana Supreme Court opinions are accepted for transfer from the Indiana Court of Appeals. *See* IND. R. APP. P. 11(B). The court's transfer docket, especially civil cases, has substantially increased in the past five years, but declined significantly last year. *See* Chief Justice Randall T. Shepard, *Indiana Law, the Supreme Court, and a New Decade*, 24 IND. L. REV. 499 (1991).

[p] Generally, the term "vacate" is used by the Indiana Supreme Court when it is reviewing a court of appeals opinion, and the term "reverse" is used when the court overrules a trial court decision. A point to consider in reviewing this table is that the court technically "vacates" every court of appeals opinion that is accepted for transfer, but may only disagree with a small portion of the reasoning and still agree with the result. *See* IND. R. APP. P. 11(B)(3). As a practical matter, "reverse" or "vacate" simply represents any action by the supreme court that does not affirm the trial court or court of appeals opinion.

[q] This does not include 37 attorney and judicial discipline opinions, 3 writs of mandamus or prohibition, or 1 opinion related to certified questions. These opinions did not reverse, vacate, or affirm any other court's decision. This also does not include 6 opinions that considered petitions for post-conviction relief.

TABLE E-2

DISPOSITION OF PETITIONS TO TRANSFER TO SUPREME COURT IN 1998[r]

	Denied or Dismissed	Granted	Total
Petitions to Transfer			
Civil[s]	292 (90.1%)	32 (9.9%)	324
Criminal[t]	367 (93.9%)	23 (6.1%)	383
Juvenile	21 (87.5%)	3 (12.5%)	24
Total	673 (92.0%)	58 (8.0%)	731

[r] This table analyzes the disposition of petitions to transfer by the court. *See* IND. R. APP. P. 11(B) This table is compiled from information provided by the Indiana Supreme Court in a report entitled, "Grant and Denial of Cases in Which Transfer to the Indiana Supreme Court Has Been Sought."

[s] This also includes petitions to transfer in tax cases and worker's compensation cases.

[t] This also includes petitions to transfer in post-conviction relief cases.

TABLE F
SUBJECT AREAS OF SELECTED DISPOSITIONS WITH FULL OPINIONS[u]

Original Actions	**Number**
• Certified Questions	1[v]
• Writs of Mandamus or Prohibition	3[w]
• Attorney Discipline	64[x]
• Judicial Discipline	1[y]
Criminal	
• Death Penalty	9[z]
• Fourth Amendment or Search and Seizure	3[aa]
• Writ of Habeas Corpus	1[bb]
Emergency Appeals to the Supreme Court	0
Trusts, Estates, or Probate	0
Real Estate or Real Property	2[cc]
Personal Property	0
Landlord-Tenant	0
Divorce or Child Support	3[dd]
Children in Need of Services ("CHINS")	0
Paternity	0
Product Liability or Strict Liability	0
Negligence or Personal Injury	4[ee]
Invasion of Privacy	0
Medical Malpractice	0
Indiana Tort Claims Act	2[ff]
Statute of Limitations or Statute of Repose	0
Tax, Department of State Revenue, or State Board of Tax Commissioners	3[gg]
Contracts	2[hh]
Corporate Law or the Indiana Business Corporation Law	1[ii]
Uniform Commercial Code	0
Banking Law	1[jj]
Employment Law	1[kk]
Insurance Law	2[ll]
Environmental Law	2[mm]
Consumer Law	1[nn]
Workers Compensation	2[oo]
Arbitration, Mediation, Alternative Dispute Resolution	0
Administrative Law	1[pp]
First Amendment, Open Door Law, or Public Records Law	1[qq]
Full Faith and Credit	0
Eleventh Amendment	0
Civil Rights	0
Indiana Constitution	14[rr]

u. This table is designed to provide a general idea of the specific subject areas upon which the court ruled or discussed and how many times it did so in 1998. It is also a quick reference guide to court rulings

for practitioners in specific areas of the law. The numbers corresponding to the areas of law reflect the number of cases in which the court substantively discussed legal issues in these subject areas. A citation list is provided in a footnote for each area.

[v] Koval v. Simon Telelect, Inc., 693 N.E.2d 1299 (Ind. 1998).

[w] State *ex rel.* W.A. v. Marion County Superior Court, Juvenile Div., 704 N.E.2d 477 (Ind. 1998); State *ex rel.* New Haven v. Allen Superior Court, 699 N.E.2d 1134 (Ind. 1998); State *ex rel.* Bishop v. Madison Circuit Court, 690 N.E.2d 1173 (Ind. 1998).

[x] *In re* Ragland, No. 49S00-9608-DI-565, 1998 WL 432963 (Ind. July 24, 1998); *In re* Nienaber, 704 N.E.2d 457 (Ind. 1998); *In re* Rabb, 704 N.E.2d 117 (Ind. 1998); *In re* Bender, 704 N.E.2d 115 (Ind. 1998); *In re* McNeil, 704 N.E.2d 114 (Ind. 1998); *In re* Comer, 704 N.E.2d 112 (Ind. 1998); *In re* Tew, 703 N.E.2d 1049 (Ind. 1998); *In re* Goebel, 703 N.E.2d 1045 (Ind. 1998); *In re* Brown, 703 N.E.2d 1041 (Ind. 1998); *In re* Campbell, 702 N.E.2d 692 (Ind. 1998); *In re* Szarwark, 702 N.E.2d 351 (Ind. 1998); *In re* Robinson, 701 N.E.2d 576 (Ind. 1998); *In re* Salter, 701 N.E.2d 576 (Ind. 1998); *In re* Hoffman, 700 N.E.2d 1138 (Ind. 1998); *In re* Riddle, 700 N.E.2d 788 (Ind. 1998); *In re* Golding, 700 N.E.2d 464 (Ind. 1998); *In re* Knobel, 699 N.E.2d 1142 (Ind. 1998); *In re* Towell, 699 N.E.2d 1138 (Ind. 1998); *In re* Puterbaugh, 699 N.E.2d 1133 (Ind. 1998); *In re* Minnette, 699 N.E.2d 1133 (Ind. 1998); *In re* Horine, 699 N.E.2d 270 (Ind. 1998); *In re* Anonymous, 698 N.E.2d 808 (Ind. 1998); *In re* Makin, 698 N.E.2d 767 (Ind. 1998); *In re* Johnston, 698 N.E.2d 313 (Ind. 1998); *In re* Radford, 698 N.E.2d 310 (Ind. 1998); *In re* O'Brien, 697 N.E.2d 479 (Ind. 1998); *In re* Newell, 697 N.E.2d 479 (Ind. 1998); *In re* Ballantine, 697 N.E.2d 478 (Ind. 1998); *In re* Ragland, 697 N.E.2d 44 (Ind. 1998); *In re* Quinn, 696 N.E.2d 863 (Ind. 1998); *In re* Szarwark, 696 N.E.2d 46 (Ind. 1998); *In re* Brooks, 695 N.E.2d 920 (Ind. 1998); *In re* Blumberg, 695 N.E.2d 114 (Ind. 1998); *In re* Pope, 695 N.E.2d 112 (Ind. 1998); *In re* Hawkins, 695 N.E.2d 109 (Ind. 1998); *In re* Merideth, 695 N.E.2d 110 (Ind. 1998); *In re* Astbury, 695 N.E.2d 98 (Ind. 1998); *In re* Chovanec, 695 N.E.2d 95 (Ind. 1998); *In re* Fletcher, 694 N.E.2d 1143 (Ind. 1998); *In re* Martenet, 694 N.E.2d 1143 (Ind. 1998); *In re* Cohen, 694 N.E.2d 1143 (Ind. 1998); *In re* Brooks, 694 N.E.2d 724 (Ind. 1998); *In re* Puterbaugh, 694 N.E.2d 281 (Ind. 1998); *In re* Bolden, 693 N.E.2d 565 (Ind. 1998); *In re* Putsey, 693 N.E.2d 565 (Ind. 1998); *In re* Thonert, 693 N.E.2d 559 (Ind. 1998); *In re* Contempt of Mittower, 693 N.E.2d 555 (Ind.1998); *In re* Barratt, 693 N.E.2d 530 (Ind. 1998); *In re* Cushing, 693 N.E.2d 530 (Ind. 1998); *In re* Haecker, 693 N.E.2d 529 (Ind. 1998); *In re* Taylor, 693 N.E.2d 526 (Ind. 1998); *In re* Antcliff, 693 N.E.2d 525 (Ind. 1998); *In re* Appointment of a Temporary Prosecuting Attorney in Knox County, 692 N.E.2d 885 (Ind. 1998); *In re* Catt, 692 N.E.2d 885 (Ind. 1998); *In re* Barnes, 691 N.E.2d 1225 (Ind. 1998); *In re* Dinius, 691 N.E.2d 1222 (Ind. 1998); *In re* Fisher, 691 N.E.2d 1221 (Ind. 1998); *In re* Colman, 691 N.E.2d 1219 (Ind. 1998); *In re* Verma, 691 N.E.2d 1211 (Ind. 1998); *In re* Neswick, 691 N.E.2d 906 (Ind. 1998); *In re* Light, 691 N.E.2d 906 (Ind. 1998); *In re* Wright, 690 N.E.2d 709 (Ind. 1998); *In re* Romero, 690 N.E.2d 707 (Ind. 1998); *In re* O'Neil, 690 N.E.2d 705 (Ind. 1998).

[y] *In re* Edwards, 694 N.E.2d 701 (Ind. 1998).

[z] Coleman v. State, 703 N.E.2d 1022 (Ind. 1998), *aff'g* (post-conviction relief); Miller v. State, 702 N.E.2d 1053 (Ind. 1998), *aff'g* (post-conviction relief); Woods v. State, 701 N.E.2d 1208 (Ind. 1998), *aff'g* (post-conviction relief); Rogers v. State, 698 N.E.2d 1172 (Ind. 1998), *aff'g* (direct appeal); Brown v. State, 698 N.E.2d 1132 (Ind. 1998), *aff'g* (post-conviction relief); Minnick v. State, 698 N.E.2d 745 (Ind. 1998), *aff'g* (post-conviction relief); Barker v. State, 695 N.E.2d 925 (Ind. 1998), *aff'g and remanding for resentencing* (direct appeal); Wisehart v. State, 693 N.E.2d 23 (Ind. 1998), *aff'g* (post-conviction relief); Johnson v. State, 693 N.E.2d 941 (Ind. 1998), *aff'g* (direct appeal).

[aa] Berry v. State, 704 N.E.2d 462 (Ind. 1998); Cox v. State, 696 N.E.2d 853 (Ind. 1998); Brown v. State, 691 N.E.2d 438 (Ind. 1998).

[bb] Sweeney v. State, 704 N.E.2d 86 (Ind. 1998).

[cc] Board of Zoning Appeals, Bloomington, Ind. v. Leisz, 702 N.E.2d 1026 (Ind. 1998); Ragucci v. Metropolitan Dev. Comm'n, 702 N.E.2d 677 (Ind. 1998).

[dd] Collier v. Collier, 702 N.E.2d 351 (Ind. 1998); Pond v. Pond, 700 N.E.2d 1130 (Ind. 1998); Lea v. Lea, 691 N.E.2d 1214 (Ind. 1998).

[ee] Hanson v. Saint Luke's United Methodist Church, 704 N.E.2d 1020 (Ind. 1998); Robinson v. Wroblewski, 704 N.E.2d 467 (Ind. 1998); Biereichel v. Smith, 704 N.E.2d 456 (Ind. 1998); Sauders v. County of Steuben, 693 N.E.2d 16 (Ind. 1998).

[ff] Indiana State Highway Comm'n v. Curtis, 704 N.E.2d 1015 (Ind. 1998); Budden v. Board of Sch. Comm'rs, 698 N.E.2d 1157 (Ind. 1998).

[gg] State Bd. of Tax Comm'rs v. Town of St. John, 702 N.E.2d 1034 (Ind. 1998); State Bd. of Tax Comm'rs v. L.H. Carbide Corp., 702 N.E.2d 706 (Ind. 1998); State Bd. of Tax Comm'rs v. Mixmill Mfg. Co., 702 N.E.2d 701 (Ind. 1998).

[hh] Indiana State Highway Comm'n v. Curtis, 704 N.E.2d 1015 (Ind. 1998); Trimble v. Ameritech Publ'g, Inc., 700 N.E.2d 1128 (Ind. 1998).

[ii] Melrose v. Capitol City Motor Lodge, Inc., 705 N.E.2d 985 (Ind. 1998).

[jj] Kirchoff v. Selby, 703 N.E.2d 644 (Ind. 1998).

[kk] McClain v. Review Bd. of Ind. Dep't of Workforce Dev., 693 N.E.2d 1314 (Ind. 1998).

[ll] Foster v. Auto-Owners Ins. Co., 703 N.E.2d 657 (Ind. 1998); Meridian Mut. Ins. Co. v. Auto-Owners Ins. Co., 698 N.E.2d 770 (Ind. 1998).

[mm] Shell Oil Co. v. Lovold Co., 705 N.E.2d 981 (Ind. 1998); Shell Oil Co. v. Meyer, 705 N.E.2d 962 (Ind. 1998).

[nn] McKinney v. State, 693 N.E.2d 65 (Ind. 1998).

[oo] Walkup v. Wabash Nat'l Corp., 702 N.E.2d 713 (Ind. 1998); Walker v. State, 694 N.E.2d 258 (Ind. 1998).

[pp] Indiana Wholesale Wine & Liquor Co. v. Indiana Alcoholic Beverage Comm'n, 695 N.E.2d 99 (Ind. 1998).

[qq] WTHR-TV v. Cline, 693 N.E.2d 1 (Ind. 1998).

[rr] Melrose v. Capitol City Motor Lodge, Inc., 705 N.E.2d 985 (Ind. 1998); Bufkin v. State, 700 N.E.2d 1147 (Ind. 1998); Robinson v. State, 699 N.E.2d 1146 (Ind. 1998); White v. State, 699 N.E.2d 630 (Ind. 1998); Anderson v. State, 699 N.E.2d 257 (Ind. 1998); Budden v. Board of Sch. Comm'rs, 698 N.E.2d 1157 (Ind. 1998); Sylvester v. State, 698 N.E. 2d 1126 (Ind. 1998); Parker v. State, 698 N.E.2d 737 (Ind. 1998); Seay v. State, 698 N.E.2d 732 (Ind. 1998); Klein v. State, 698 N.E.2d 296 (Ind. 1998); Wilson v. State, 697 N.E.2d 466 (Ind. 1998); Ajabu v. State, 693 N.E.2d 921 (Ind. 1998); Ratliff v. Cohn, 693 N.E.2d 530 (Ind. 1998); WTHR-TV v. Cline, 693 N.E.2d 1 (Ind. 1998).

1998 Bankruptcy Law Update for Seventh Circuit Practitioners

Timothy A. Ogden*

Introduction

The Seventh Circuit Court of Appeals wrote a number of interesting, and in some cases entertaining, decisions in the area of bankruptcy law. This Article examines some of those decisions.

I. Equitable Subordination of Claims

In re Lifschultz Fast Freight[1] involved a request by the bankruptcy trustee to equitably subordinate a creditor's secured claim.[2] The bankruptcy court denied this request, but the district court reversed and remanded.[3] The issue on appeal was whether the bankruptcy court could exercise its power of equitable subordination based on the debtor's purported undercapitalization.[4] In this case, Lifschultz Fast Freight Corporation (the "debtor"), developed from another company, Lifschultz Fast Freight, Inc. ("LFFI"), which had operated in the shipping industry since the beginning of the century.[5] LFFI suffered tremendous losses in the late 1980s (which approached $5.5 million in 1989). In an effort to save the business, the owners established the company that would become the debtor. Five individuals (the "insiders") held eighty percent of the debtor's stock, and LFFI held the remaining twenty percent.[6]

From the outset, the debtor was cash poor. Thus, just weeks after its inception, one of the insiders' affiliated companies, Salson Express, entered into a secured loan agreement with the debtor. Essentially, three of the insiders offered personal guarantees for money they borrowed from First Fidelity Bank. They then lent that money to Salson Express, which in turn lent the money to the debtor. Within one month, the debtor had borrowed more than $862,000 from Salson Express.[7] Significantly, the debtor also obtained another $1 million

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* Partner, Ogden & Ogden, LLP, Warsaw. Associate Professor, Accounting and Business, Manchester College. B.A., *with distinction*, 1987, Manchester College; M.B.A., 1989, Peter F. Drucker Graduate Management Center, Claremont Graduate School; J.D., *summa cum laude*, 1996, Indiana University.

1. 132 F.3d 339 (7th Cir. 1997).

2. "Equitable subordination of a claim moves the creditor down in the order of payment out of the assets in the bankruptcy estate, generally reducing (or eliminating) the amount the creditor can recover." *Id.* at 341. After notice and a hearing, the court may "under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim . . . ." 11 U.S.C. § 510(c)(1) (1994).

3. *In re Lifschultz*, 132 F.3d at 341.

4. *See id.* at 343.

5. *See id.* at 342.

6. *See id.*

7. *See id.*

through a factoring agreement with Ambassador Factors.[8] This new money permitted the debtor to pay off all but $300,000 of the insiders' secured loan.[9] The insiders filed a claim in bankruptcy for the $300,000, and the trustee argued that the secured interest should be equitably subordinated.[10]

The bankruptcy court concluded that the debtor had not been undercapitalized and that even if it had, equitable subordination required some other inequitable conduct.[11] The district court, however, decided that undercapitalization alone was sufficient to justify invoking the doctrine of equitable subordination and concluded that the debtor was "patently undercapitalized."[12]

The court of appeals noted that one important theme of bankruptcy law is maintaining claimants' state law rights and the order of their claims relative to one another.[13] The potential always exists for an equity holder, who comes last on the priority list, to "dress[ ] up a claim she has on the firm as something else of higher priority."[14] However, it may be even more likely in bankruptcy cases involving closely held corporations because the players' roles may be less distinct: "[T]he same person can be an owner of a company, its creditor and, as in the instant case, its employee as well."[15] Nevertheless, insiders must remain true to their fiduciary obligations to the company.[16] If they breach those duties through a bad faith or unfair characterization of an equity infusion as debt, the court may send the insiders to the end of the line.[17]

The court in *Lifschultz* relied on the framework provided by the U.S. Court of Appeals for the Fifth Circuit in *In re Mobile Steel Co.*[18] The first step under that framework is to search for inequitable conduct, and if there is none, the bankruptcy court may not subordinate the claim.[19] The court proceeded through a detailed discussion of undercapitalization and whether the fact of undercapitalization alone would constitute such misconduct. While recognizing that some courts have adopted this position,[20] this court chose not to do so.

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8. The agreement with Ambassador Factors required that its interest be superior to the insiders' interest under the secured loan agreement, and Ambassador also received personal guarantees from the insiders. *See id.*

9. The court referred to Salson Express and the insiders interchangeably. *See id.* at 343.

10. *See id.*

11. *Id.*

12. *Id.* The debtor was set up with $1000 in cash, and the insiders also transferred to the debtor all of LFFI's operations outside New York, including its customer list, a valuable lease to a California shipping terminal, and Los Angeles Dodgers season tickets. *See id.* at 342.

13. *Id.* at 343.

14. *Id.*

15. *Id.* at 344.

16. *See id.*

17. *See id.*

18. 563 F.2d 692 (5th Cir. 1977).

19. *See In re Lifschultz,* 132 F.3d at 344.

20. *Id.* at 345 (citing, e.g., *In re* Fabricators, 926 F.2d 1458, 1470 (5th Cir. 1991)).

"Because mere undercapitalization does not, and should not, justify equitable subordination, we think the better view is that, while undercapitalization may indicate inequitable conduct, undercapitalization is not in itself inequitable conduct."[21]

This was not a case where the insiders attempted to convert already existing equity into debt. They contributed fresh capital, and if no deception existed, there was no reason to treat an insider's loan more harshly than a third party's loan.[22] The court summarized its position as follows: "[U]ndercapitalization alone, without evidence of deception about the debtor's financial condition or other misconduct, cannot justify equitable subordination of an insider's debt claim. Extraordinary circumstances might provide an exception . . . but we believe that almost any such exception would arguably also involve other misconduct of some sort."[23]

The court also addressed the debtor's purported undercapitalization itself and concluded that under *Mobile Steel*, undercapitalization would have existed at the time the debtor received the loan from the insiders if an informed outside source would not also have loaned the debtor a similar amount of money.[24] "In this case, we need not speculate about what might have happened. We know what *did* happen. The debtor not only could have gotten a third-party loan, it actually did—from Ambassador Factors."[25] Furthermore, that Ambassador Factors required personal guarantees from several insiders did not prove undercapitalization.[26] Thus, the court found no clear error in the bankruptcy court's factual conclusion.[27]

Interestingly, however, the court still remanded the case.[28] The trustee had also argued, among other things, that the insiders had inflated their salaries in the spring and summer before the bankruptcy petition was filed. The court noted that a "classic form of creditor misconduct is boosting the owner-employee's salary as the firm is drifting into financial collapse."[29] If an insider did commit such misconduct, it could justify equitable subordination of the Salson Express claim.[30] The court remanded the case so that the bankruptcy court could determine whether the insiders could meet their burden of showing that the transactions were inherently fair and were undertaken in good faith.[31]

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21. *Id.* "Most often undercapitalization signifies nothing more than business failure, poor access to capital, or both." *Id.*

22. *Id.* at 347.

23. *Id.* at 349 (citations omitted).

24. *Id.* at 351 (citing *In re* Mobile Steel Co., 563 F.2d 692, 703 (5th Cir. 1997)).

25. *Id.* at 353.

26. *See id.*

27. *Id.*

28. *Id.* at 355.

29. *Id.* at 354.

30. *See id.*

31. *Id.* at 354-55.

II. Cases Involving the Geraci Firm

A. Unjustified High Fees

Attorney Peter Francis Geraci and the associates in his firm (the "Geraci firm") file thousands of bankruptcy cases each year in the Seventh Circuit,[32] and the firm's practices provide the judges on the court of appeals with a number of opportunities to earn their salaries. *In re Geraci*[33] dealt with twelve consumer bankruptcy cases in which the Geraci firm had represented the debtors. The cases were relatively straightforward and required little attorney time. In fact, the attorneys spent an average of only thirty-six minutes preparing each petition,[34] yet the Geraci firm charged a flat fee ranging from $1095 to $1900 in each.[35] "Believing that those fees were unreasonably high in light of the uncomplicated nature of the cases at issue, the United States Trustee invoked Bankruptcy Rule 2017 to challenge the fees charged . . . ."[36]

Bankruptcy Judge Fines analyzed the criteria listed in 11 U.S.C. § 330 regarding compensation of professionals by considering the twelve factors set out in *Johnson v. Georgia Highway Express, Inc.*[37] The bankruptcy court found that the average fee charged in similar cases in that location was $550 and that neither the Geraci firm's experience and ability nor the results obtained justified significantly higher fees.[38] The bankruptcy court concluded that $800 was presumptively reasonable and ordered Geraci to return to each of the twelve debtors the portion of each fee that exceeded $800. The court also made the order applicable to all future cases filed by that law firm in that court, which meant that "Geraci either could accept a presumptively reasonable fee of $800 in no-asset consumer bankruptcy cases under Chapter 7, or file a detailed fee itemization in support of a higher fee."[39]

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32. *See In re* Turner, 156 F.3d 713, 715 (7th Cir. 1998).

33. 138 F.3d 314 (7th Cir. 1998).

34. *See id.* at 319.

35. *See id.* at 316.

36. *Id.* at 317.

37. 488 F.2d 714, 717-19 (5th Cir. 1974).

38. *In re Geraci*, 138 F.3d at 317. In fact, despite Geraci's description of himself as the "'foremost consumer bankruptcy practitioner in the country,'" Judge Fines concluded that "[t]he work product of [the Geraci firm] is not extraordinary. It is not outstanding. It is not up to a level that this [c]ourt sees from the majority of practitioners who regularly appear before it." *Id.* at 317-18.

39. *Id.* at 318. The trustee brought similar challenges in other bankruptcy courts throughout Illinois, and those challenges resulted in orders similar to the one at issue here. Geraci informed the court that "fee orders in 72 cases already have been appealed to this court and that approximately 400 more appeals are on their way." *Id.* at 318 n.3. Later, in the case *In re Agnew*, 144 F.3d 1013 (7th Cir. 1998), other bankruptcy judges in the same district determined that $575 and $600 were presumptively reasonable fees, and the Seventh Circuit affirmed. *Id.* at 1014. The court stated that judges and trustees were pushed to take this approach to handling fees

Geraci made a number of arguments on appeal, but to no avail. Geraci argued that he was entitled to the market value of his services and that the market value was whatever he was able to negotiate with his clients. The court disagreed, stating that sections 329 and 330 of the Bankruptcy Code limit the market's role in establishing professional fees in bankruptcy cases.[40] There is no requirement that there be overreaching by debtor's counsel or that there be no arm's length transaction to check the reasonableness of the agreed-to fee in order for the bankruptcy court to exercise its power of review, as Geraci contended.[41] "Rather, the bankruptcy court is authorized to act whenever it determines that the compensation the debtor has paid or agreed to pay his counsel exceeds the reasonable value of the services provided."[42]

The court also found that the bankruptcy court did not arbitrarily cap Geraci's fees because Geraci maintained the right to demonstrate that the services provided justify a higher fee.[43] Moreover, even if Geraci had not waived his Equal Protection Clause argument by failing to raise it in the bankruptcy court, he would not have prevailed.[44] The record indicated that Judge Fines used the same presumption of a reasonable fee in all similar cases before him.[45] The Seventh Circuit therefore affirmed.[46]

B. Unilateral Reaffirmation of Pre-Petition Debts

Another case involving the Geraci firm, *In re Turner*,[47] addressed the situation where the debtor unilaterally reaffirmed a pre-petition debt. The court of appeals agreed with the lower courts that such a reaffirmation did not

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> by a perception that Geraci conducts his practice in an abusive manner, taking advantage of debtors who are unaware that his promises of superior services at a premium rate are hot air (one bankruptcy judge found that 'Geraci's work is not on a par with that of other bankruptcy practitioners, that his motions practice leaves much to be desired, and that his abilities as a trial lawyer are substandard') . . . .

Id.

40. *In re Geraci*, 138 F.3d at 320 (referring to 11 U.S.C. §§ 229, 330 (1994)).

41. *See id.*

42. *Id.*

43. *Id.* at 321.

44. *See id.*

45. *See id.*

46. *Id.* Geraci was also involved in another appeal to the Seventh Circuit, *In re Bryson*, 131 F.3d 601 (7th Cir. 1997). There, Geraci's client fired the Geraci firm and sought to have unearned fees returned. The bankruptcy judge ordered Geraci to return to Bryson $182.50. Geraci, of course, appealed. The district court found that Geraci filed a motion to reconsider in bad faith as a vehicle for extending the time available for appeal, and it granted Bryson's motion to dismiss. *Id.* at 602-03. The court of appeals reversed, opining that the court had more appropriate methods available for dealing with a bad faith motion to reconsider. *Id.* at 603.

47. 156 F.3d 713 (7th Cir. 1998).

constitute an "agreement" for purposes of 11 U.S.C. § 524(c).[48] In each of the six bankruptcy cases underlying the appeal, the Geraci firm had filed a document entitled "REAFFIRMATION AGREEMENT" or "AUTOMOBILE REAFFIRMATION AGREEMENT" whereby the debtor purportedly agreed to pay a pre-petition installment debt.[49] In each case, the debtor, but not the creditor, signed the reaffirmation.[50] The Geraci firm filed these "agreements" without even notifying the creditors of their execution.[51]

The bankruptcy court concluded that strict compliance with section 524 of the Bankruptcy Code was mandatory and that the creditor's signature was required in order to comply with that section.[52] Bankruptcy Judge Fines further stated that "[r]eaffirmation agreements are unlike any other contractual agreement under the law, . . . and nowhere else is the requirement that both parties sign the agreement more critical."[53] The signature demonstrates not only that the creditor is aware of the reaffirmation, but also that there is agreement between the parties.[54]

The appeals court noted that in canvassing the U.S. Trustees and their field offices, none saw these types of reaffirmation agreements outside this circuit's judicial districts, and within this circuit, the only such reaffirmations the trustees encountered were filed by the Geraci firm.[55] The court emphasized the statute's repeated reference to an "agreement" and noted that "[a]s unilateral statements of reaffirmation, filed without notice to the creditors, let alone their consent, the declarations at issue here cannot be understood as the mutual 'agreement' that the statute requires."[56] The court also recognized that even though section 524(c) does not expressly require the creditor's signature, the bankruptcy court's reasoning in requiring such was not assailable.[57] That signature provides concrete evidence of the creditor's awareness of and assent to the terms of the reaffirmation.[58]

III. Letters of Credit and Voidable Preferences

In re Bergner[59] was a relatively complicated case where Bergner made payments (shortly before declaring bankruptcy) to Bank One in order to cover the

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48. *Id.* at 721.
49. *See id.* at 715.
50. *See id.*
51. *See id.*
52. *See id.*
53. *See id.* (internal quotes omitted).
54. *See id.* at 720.
55. *Id.* at 716.
56. *Id.* at 719.
57. *Id.* at 720.
58. *See id.*
59. 140 F.3d 1111 (7th Cir. 1998).

bank's payments honoring certain letters of credit.[60] Bergner later sought to recover those payments as voidable preferences under 11 U.S.C. § 547(b). The Seventh Circuit affirmed the district court's determination that the payments were voidable preferences, but reversed on the issue of prejudgment interest.[61] The denial of such interest was an abuse of discretion, and the case was remanded to determine the appropriate amount of interest due.[62]

At Bergner's request, Bank One issued standby letters of credit to AMC, one of Bergner's suppliers, and to Liberty Mutual Insurance, an insurance provider.[63] As long as Bergner paid these creditors, the letters of credit did not come into play. However, the occurrence of certain events would entitle AMC and Liberty Mutual (the beneficiaries) to go straight to Bank One for payments on Bergner's promises without regard to Bergner's financial health.[64] One of those events was a decision by Bank One not to renew the letters of credit upon their expiration.[65]

By mid-summer 1991, Bank One had issued letters of credit exceeding $31.2 million to AMC and exceeding $5.8 million to Liberty Mutual.[66] When Bank One informed Bergner and these two beneficiaries that it would not renew the letters of credit upon their expiration at the end of July, AMC notified Bergner that it intended to exercise its rights under the agreement and draw down the full amount of its credit. Bergner relied on a revolving line of credit (totaling approximately $74 million) that it had with a Swiss bank group to fund AMC's draw from Bank One.[67]

Bergner's financial position continued its downward spiral, however, and the Swiss bank group eventually pulled the remaining $43 million line of credit.[68] Bank One exercised its rights under the Standby Letter of Credit Agreement and took control of funds in Bergner's account to satisfy future claims by Liberty Mutual under its letter of credit. That same day, Bergner filed a Chapter 11

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60. *See id.* at 1114.

61. *Id.* at 1123.

62. *See id.*

63. *See id.* at 1114.

64. Bergner was paying Bank One approximately $300,000 per year for this service. *See id.* at 1115. In addition, the Standby Letter of Credit Agreement between Bergner and Bank One, which established the terms of the agreement between these two parties, required Bergner to pay Bank One the amount of any draft presented by a beneficiary either before or at the time of presentation to Bank One for payment. *See id.*

65. It is important to note that the relationships in letter of credit arrangements are independent of one another. For example, if an event occurred that permitted a beneficiary to draw on the letter of credit, Bank One would be required to pay the beneficiary without regard to Bergner's obligations to Bank One. If Bergner breached his duty to pay Bank One under the Standby Letter of Credit Agreement, Bank One would have a valid contract action against Bergner, but it would be no less obligated to honor its contractual duty to the beneficiary. *See id.* at 1119, 1114.

66. *See id.* at 1115.

67. *See id.* at 1116.

68. *See id.*

petition for bankruptcy.[69]

The central issue in this case was whether the lower courts concluded correctly that Bergner's payments to Bank One to cover the AMC and Liberty Mutual obligations were voidable preferences under section 547(b) of the Bankruptcy Code.[70] Bank One argued that it was only a collection agent for Bergner, that the money simply flowed through the bank, and therefore if Bergner were to recover these payments, it would receive a windfall.[71] The problem was that "Bank One's position [did] not reflect the independent obligations that ran from the bank to the beneficiaries."[72]

> Thus, when AMC presented its draft with conforming documents to Bank One on July 19, 1991, Bank One was required to pay AMC the full $31,207,000 that the letter of credit then provided, whether or not Bergner gave it a red cent. If Bergner did not comply with its own agreement with Bank One, under which it was required to give the bank the amount of the draw either before or at the time of the payment to the beneficiary, then Bank One would have had a perfectly good contract action against Bergner, but it would have had no defense against honoring the beneficiary's demand.
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> This means that at the moment AMC presented its draft, a debt arose between Bergner (as debtor) and Bank One (as creditor), in the amount of the requested draft.[73]

The Seventh Circuit concluded that Bank One's arguments were simply unpersuasive attempts to recharacterize the transaction and to attack the independence principle.[74] The elements of section 547(b) were all present, and the transfers were thus voidable preferences.[75]

IV. State Claim for Support of Delinquent Minor

In re Platter[76] involved a debtor whose delinquent son was placed in a residential treatment facility. Under Indiana Code section 31-6-4-18(b),[77] the

69. *See id.*
70. *Id.* at 1118.
71. *See id.* at 1118-19.
72. *Id.* at 1119.
73. *Id.* (citations omitted).
74. *Id.* at 1120.
75. *See id.* at 1119-20.
76. 140 F.3d 676 (7th Cir. 1998).
77. In 1997 Indiana lawmakers repealed this section and replaced it with Indiana Code section 31-40-1-2, which provides: "The child's parent or the guardian of the estate of a child shall reimburse the county for the costs paid under subsection (a) (or [Indiana Code section] 31-6-4-

mother was required to repay the $65,565 cost incurred by the DeKalb County Division of Family and Children Services ("DFCS") in caring for her son.[78] When Platter declared bankruptcy, DFCS argued that this obligation was not dischargeable.[79] Despite the divided authority on this issue, the bankruptcy court held Platter's debt dischargeable, and the District Court for the Northern District of Indiana affirmed.[80]

The first issue on appeal dealt with DFCS's purported immunity under the Eleventh Amendment.[81] DFCS argued that the bankruptcy court had no authority to determine whether Platter's debt to the state agency was dischargeable.[82] "For over a century, the Supreme Court has interpreted the Amendment to deny to the federal courts authority to entertain a suit brought by a private party against a state without its consent."[83] The court dealt with the issue summarily, however, concluding that "[b]ecause a state voluntarily chooses to enter a bankruptcy case when it initiates an adversary proceeding, we hold that a state removes itself from the Eleventh Amendment's protection by starting one."[84] A state cannot enter a federal forum voluntarily and then seek protection under the Eleventh Amendment just because it does not like the result.[85]

The second issue in the *Platter* case dealt with discharge of the debt. DFCS relied upon section 523(a)(5) of the Bankruptcy Code.[86] This section provides that a discharge does not discharge the debtor from a debt

> to a spouse, former spouse, or child of the debtor, for alimony to, maintenance for, or support of such spouse or child, . . . but not to the extent that . . . such debt includes a liability designated as alimony, maintenance, or support, unless such liability is actually in the nature of alimony, maintenance, or support.[87]

This debt was not owed to the spouse, former spouse or child. Therefore, the Code section that DFCS relied on was inapplicable, and the debt could be discharged.[88] Further, the court reviewed Congress' 1984 amendment to the

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before its repeal) as provided under this article." IND. CODE § 31-40-1-2(c) (1998).

78. *In re Platter*, 140 F.3d at 678.

79. *See id.*

80. *Id.*

81. *See id.* "The Eleventh Amendment provides that the Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." *Id.* (quoting U.S. CONST. amend. XI).

82. *See id.* at 679.

83. *Id.* at 678 (citing Hans v. Louisiana, 134 U.S. 1, 15 (1890)).

84. *Id.* at 679.

85. *See id.* at 680.

86. *See id.* at 680-81.

87. 11 U.S.C. § 523(a)(5) (1994 & Supp. III 1997).

88. *See In re Platter*, 140 F.3d at 681.

Code section at issue along with the relevant legislative history.[89] The court concluded that DFCS's position was not supported.[90]

V. Allocation of Taxes Between Landlord and Bankrupt Tenant

The Seventh Circuit decided an important issue last year that had been addressed by numerous lower courts but not by a court of appeals. *In re Handy Andy Home Improvement Centers, Inc.*[91] answered whether the bankrupt tenant's debt to the landlord for taxes paid had to be prorated or whether it was entirely a post-petition debt.[92] The Seventh Circuit affirmed the lower court decisions that the debt had to be prorated, and it clarified that "the dividing line is . . . not the date on which the petition is filed but the date on which the order for relief is entered."[93]

In Cook County, Illinois, taxpayers are billed after the period of assessment, and as elsewhere, landlords often pay the taxes as they come due and are later reimbursed by their tenants.[94] The landlord in this case, National Terminals Corporation ("National"), received the bill for the second installment of 1994 taxes in September 1995. In October 1995, tenant Handy Andy's creditors filed an involuntary petition for bankruptcy. An order for relief, pursuant to 11 U.S.C. § 303(h), was entered on November 1, 1995.[95] Two weeks after the petition was filed but before the order for relief was entered, National paid the tax bill and invoiced Handy Andy. In February 1996 National received and paid the tax bill for the first installment of 1995 taxes, and it invoiced Handy Andy again. Handy Andy rejected the lease in April 1996.[96]

Post-petition creditors receive high priority in the distribution of the debtor's estate;[97] moreover, section 365(d)(3) of the Bankruptcy Code provides that the trustee or the debtor in possession "shall timely perform all the obligations of the debtor, . . . arising from and after the order for relief under any unexpired lease of nonresidential real property, until such lease is assumed or rejected . . . ."[98] National argued that Handy Andy's obligation under the lease was a post-petition debt—that it could not have arisen until the billing date for tax reimbursement, (i.e., the rental due date after National paid the county taxes).[99] The court disagreed.[100]

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89. *Id.* at 681-82.
90. *Id.* at 683.
91. 144 F.3d 1125 (7th Cir. 1998).
92. *Id.* at 1126.
93. *Id.*
94. *See id.*
95. *See id.*
96. *See id.*
97. *See id.* at 1127.
98. 11 U.S.C. § 365(d)(3) (1994).
99. *See In re Andy*, 144 F.3d at 1126-27.
100. *Id.*

Handy Andy's debt related entirely to an earlier period and was therefore no different from debts to trade creditors incurred in 1994 but never paid.[101]

> A trade creditor does not, by virtue of continuing to sell to the debtor after the latter has gone into bankruptcy, obtain a priority for what the debtor owes him for goods or services sold to the debtor before the bankruptcy. National is in no different situation by virtue of section 365(d)(3).[102]

The court opted for an interpretation of the statute that would not "make the rights of creditors turn on the happenstance of the dating of tax bills and the strategic moves of landlords and tenants."[103]

VI. Discharge of Marital Obligations and the Burden of Proof

In the Seventh Circuit case *In re Crosswhite*,[104] the Crosswhites divorced, and Mr. Crosswhite ("husband") agreed to assume and to hold Ms. Ginter ("wife") harmless on two joint debts. Husband did not pay the debts but instead declared bankruptcy.[105] Wife paid one of the debts, and she restructured the other and made payments on it. She then initiated an adversary proceeding in husband's bankruptcy to determine whether husband's obligation under the property settlement was dischargeable under 11 U.S.C. § 523(a)(15).[106] The bankruptcy court held the obligations were dischargeable, and the district court affirmed.[107] Wife appealed.[108]

Section 523(a)(15) of the Bankruptcy Code provides that an individual is not discharged from any debt "not of the kind described in paragraph (5) that is incurred by the debtor in the course of a divorce or separation or in connection with a separation agreement, divorce decree or other order of a court of record . . . unless" one of two conditions exists.[109] The debt is dischargeable if "the debtor does not have the ability to pay the debt from disposable income, or . . . the benefit to the debtor in discharging the debt outweighs the detrimental

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101. *See id.* at 1127-28.

102. *Id.* at 1128. The court also noted that section 365(d)(3) establishes the date of the order for relief as the cutoff. *Id.* at 1127. Any obligation arising before that date would not fall within this section. Here, that date was November 1, 1995. *Id.* at 1126. National received a bill, paid it, and invoiced Handy Andy for the second installment of the 1994 taxes before November 1, 1995. In no case, then, could that obligation have arisen after the order for relief. However, the court did not rely on this line of reasoning because Handy Andy did not. *Id.* at 1127.

103. *Id.* at 1128.

104. 148 F.3d 879 (7th Cir. 1998).

105. *See id.* at 881.

106. *See id.*

107. *See id.*

108. *See id.*

109. 11 U.S.C. § 523(a)(15) (1994).

consequences to the debtor's former spouse or child."[110] The bankruptcy court held that, despite husband's "'somewhat parasitic existence,'" it was appropriate to discharge the debt because the benefit to husband outweighed the detriment to wife.[111]

Wife did not object to carrying the initial burden of showing the existence of a nondischargeable debt—one that was incurred by the debtor pursuant to a divorce but did not fall under section 523(a)(5). Instead, she contended that the court incorrectly failed to place on husband, the debtor, the burden of establishing an affirmative defense—either that he could not pay the debt or that the benefit to him of discharge outweighed the detriment to wife of no discharge.[112]

The Seventh Circuit concluded that "there is a clear shift in the burden of proof under [section] 523 (a)(15). The burden of proving initially that she holds a subsection (15) claim against the debtor should be borne by the creditor (nondebtor/former spouse)."[113] Once the creditor has overcome this hurdle, "the burden of proving that he falls within either of the two exceptions to nondischargeability rests with the debtor."[114]

The court stated that both the bankruptcy court and the district court "appeared to acknowledge, at one point, that the burden of establishing the exception is on the debtor."[115] Nonetheless, the court vacated the decision and remanded it,[116] because "a reading of both opinions in their entirety leaves us with grave doubt as to whether abstract verbalization of the correct standard actually was applied in the courts' analyses . . . . Rather, it appears to us that these courts may well have placed improperly the burden of satisfying the test under [section] 523(a)(15)(B) on the creditor, [wife], rather than on the debtor, [husband]."[117] The dissent disagreed.[118]

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110. *In re Crosswhite*, 148 F.3d at 883 (citing 11 U.S.C. § 523(a)(15)(A)-(B)).
111. *Id.* at 883-84.
112. *See id.* at 884.
113. *Id.*
114. *Id.* at 884-85.
115. *Id.* at 886.
116. *Id.* at 889.
117. *Id.* at 886.
118.

> Both of the lower courts stated the appropriate burden of proof, but this court remands because it questions whether they actually applied that burden. I conclude that they did apply the burden they recited, leaving the key question of whether the bankruptcy court abused its discretion in balancing the harms under (a)(15)(B) in favor of [husband]. In my view it did not, and therefore, I would affirm.

Id. at 890 (Manion, J., dissenting).

VII. Discretion to Deny Fees

In re Crivello[119] addressed the issue of compensating professionals employed in the bankruptcy who, as discovered later, were not disinterested. Crivello, the debtor in possession, sought to retain Kravit, Gass & Weber, S.C. ("KGW") as his bankruptcy counsel.[120] KGW failed to disclose earlier dealings it had with the debtor, and it failed to disclose pre-petition claims it held against him.[121]

When KGW later applied to the bankruptcy court for final compensation of more than $334,000, the U.S. Trustee objected, arguing that "KGW was not disinterested, that KGW failed to disclose its connections to insiders adequately, and that the amount of the request was unreasonable."[122] After KGW filed an amended affidavit of disinterestedness explaining why certain facts had not been included in the original affidavit, the bankruptcy court revoked the firm's order of employment and denied its request for compensation entirely.[123] The district court affirmed.[124]

The court of appeals discussed the issue of professional compensation as a backdrop to its determination of the question "whether a bankruptcy court must deny fees when it subsequently learns that a professional never should have been employed under [section] 327(a) in the first place or whether it has *discretion* to deny fees."[125]

The U.S. trustee relied on the holding in the case *Michel v. Federated Department Stores, Inc.*,[126] in support of a mandatory denial of fees. The Seventh Circuit rejected the trustee's argument based on the plain language of the statute.[127] Section 328(c) states that the court "may deny allowance of compensation . . . if, at any time during such professional person's employment . . . such professional person is not a disinterested person, or represents or holds an interest adverse to the interest of the estate with respect to the matter on which such professional person is employed."[128]

The court stated that in order to reach the trustee's conclusion, it would have to interpret the word "is" in section 328(c) to mean "becomes," and it would have to insert the word "valid" before the word "employment."[129] This the court refused to do.[130] "Under the plain language of the provision, [section] 328(c) covers questions about whether this erroneously employed professional merits

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119. 134 F.3d 831 (7th Cir. 1998).
120. *See id.* at 833.
121. *See id.* at 834.
122. *Id.*
123. *See id.* at 834-35.
124. *See id.* at 835.
125. *Id.* at 836 (emphasis in original).
126. 44 F.3d 1310 (6th Cir. 1995).
127. *In re Crivello*, 134 F.3d at 837.
128. 11 U.S.C. § 328(c) (1994).
129. *In re Crivello*, 134 F.3d at 837.
130. *Id.*

compensation. Thus a bankruptcy court has discretion in denying that professional's fees."[131]

VIII. Two Other Decisions Worth Mentioning

In re Linton[132] involved a situation where a party wanted to sue a bankruptcy trustee in state court after the bankruptcy proceeding had been closed. Betty Lasiter and Richard Scharpf sought leave from the bankruptcy court to sue the trustee Paul Gresk for malicious prosecution of an adversary action he filed against them while the bankruptcy proceeding was pending.[133] The bankruptcy court denied the motion, and both the district court and the court of appeals affirmed.[134]

Although the court did not find any federal appellate court cases addressing the requirement for leave after the bankruptcy is closed, it concluded such leave to sue the trustee is required.[135] The rationale for the requirement during bankruptcy also applies after the bankruptcy has been wound up (e.g., if the trustee "is burdened with having to defend against suits by litigants disappointed by his actions on the court's behalf, his work for the court will be impeded"; and "it will be harder for courts to find competent people to appoint as trustees").[136]

In *In re Greenig*[137] the Greenigs submitted and the bankruptcy court confirmed their Chapter 12 reorganization plans. The plans listed United Feeds as a creditor holding an allowed claim, but United Feeds failed to file the required proof of claim before the deadline passed.[138] When United Feeds did not receive its first payment from the Greenigs under the reorganization, it filed a motion for leave to file a late proof of claim. The bankruptcy court granted the motion, but the district court reversed.[139]

The Seventh Circuit affirmed the district court's decision.[140] A bankruptcy court does not possess the equitable power to permit a new claim that is filed

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131. *Id.* Nevertheless, the court of appeals reversed the district court and remanded the case to the bankruptcy court because the "bankruptcy court's erroneous findings of fact may have tainted its discretion." *Id.* at 839. The district court found no support in the record for the bankruptcy court's determination "that KGW attempted to thwart the Code's disclosure requirements and that KGW willfully failed to disclose its prior representation." *Id.* at 840. Because the district court did not consider whether these erroneous findings may have tainted the lower court's exercise of discretion, the court of appeals was obligated to reverse. *Id.*

132. 136 F.3d 544 (7th Cir. 1998).

133. *See id.* at 544-45.

134. *Id.* at 544, 547.

135. *Id.* at 545.

136. *Id.*

137. 152 F.3d 631 (7th Cir. 1998).

138. *See id.* at 632.

139. *See id.* at 633.

140. *Id.* at 636.

late.[141] This is different from a Chapter 11 case where a proof of claim may be deemed filed if the debt is scheduled.[142] "In a Chapter 12 bankruptcy case, the creditor has [ninety] days to file a proof of claim, unless an exception of [Federal Rule of Bankruptcy Procedure] 3002(c) applies. This requirement may not be circumvented, either by the existence of a confirmed plan, or by the presence of equitable considerations."[143]

CONCLUSION

These decisions address important questions for Indiana practitioners. Next year at this time, attorneys will likely be reading not only about important developments in the case law, but also significant changes in the Bankruptcy Code itself.

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141. *See id.* at 635.
142. *See id.* at 633.
143. *Id.* at 636.

1998 UPDATE OF FEDERAL CIVIL PRACTICE FOR SEVENTH CIRCUIT PRACTITIONERS*

JOHN R. MALEY**

INTRODUCTION

Federal practitioners encountered continued changes during 1998 in federal civil practice. New opinions from the Seventh Circuit and the local district courts refined jurisdictional and procedural precedent, and local rule changes in the Southern District of Indiana effective January 1, 1999, will significantly impact local summary judgment practice. This Article outlines these important developments. For ease of future reference, topics are presented in the order they often arise in federal litigation.

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* The contents of this Article were previously published in substantial part in John R. Maley, *Procedural Issues Continue to Impact Local Federal Practice*, IND. LAW., Mar. 17-Mar. 30, 1999, at 5.

** Partner, Barnes & Thornburg, Indianapolis. B.A., 1985, University of Notre Dame; J.D., *summa cum laude*, 1988, Indiana University School of Law—Indianapolis; M.B.A., 1994, Indiana University; Chair, Local Rules Advisory Committee, U.S. District Court, Southern District of Indiana.

I. PLEADINGS/EARLY MOTIONS PRACTICE

A. Amount in Controversy

In *Herremans v. Carrera Designs*,[1] the Seventh Circuit reaffirmed that for determining the $75,000-plus minimum amount in controversy for diversity jurisdiction, individual plaintiffs can aggregate their separate claims or counts to meet the minimum. This is because 28 U.S.C. § 1332(a) jurisdiction exists over "civil actions," not over counts.[2]

B. Diversity of Citizenship

In *51 Associates Ltd. Partnership v. Associated Business Telephone Systems*,[3] the Seventh Circuit requested jurisidicational memoranda addressing whether diversity jurisdiction existed. The court dismissed the appeal with instructions for the district court to dismiss the case as non-diverse.[4] Because the plaintiff was a limited partnership, the citizenship of every partner—general and limited—was necessary to establish diversity jurisdiction under the Supreme Court's decision in *Carden v. Arkoma Associates*,[5] but because the record was silent as to the limited partners' citizenship, dismissal was required.[6]

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1. 157 F.3d 1118 (7th Cir. 1998).
2. *See id.* at 1121; 28 U.S.C. § 1332(a) (1994 & Supp. II 1996).
3. No. 98-2547, 1998 WL 911700 (7th Cir. Dec. 28, 1998).
4. *Id.* at *1.
5. 494 U.S. 185 (1990).
6. *51 Assoc. Ltd. Partnership*, 1998 WL 911700, at *1.

C. Transfer

In *North Shore Gas Co. v. Salomon, Inc.*,[7] appellant asserted error in the district court's refusal to transfer the action to another district court pursuant to 28 U.S.C. § 1404. The Seventh Circuit quickly disposed of that argument, noting the issue "does not warrant extended discussion" because district courts have "broad discretion" on motions to transfer under § 1404(a), and reversal lies only for a clear abuse of that discretion.[8] This is an important reminder to practitioners seeking transfer, who are more often than not unsuccessful in these motions.

D. Joining Insignificant Employees as Defendants

In *Latimore v. Citibank Federal Savings Bank*,[9] plaintiff sued Citibank and two of its employees under the Equal Credit Opportunity Act and Fair Housing Act. Summary judgment was granted for the defendants. On appeal, in the midst of a lengthy opinion addressing various substantive issues, Chief Judge Posner commented on the panel's "displeasure" that the plaintiff joined one of the individual defendants in the case.[10] Noting that there was no evidence supporting a claim against the individual, Judge Posner wrote:

> But as the [defense] lawyers do not ask for sanctions for the filing of a frivolous claim against [the individual], we shall let the matter drop with a warning that this court does not look with favor on the promiscuous joinder of minor employees as defendants in cases against their employers.[11]

E. Affirmative Defenses

In *Brunswick Leasing Corp. v. Wisconsin Central Ltd.*,[12] Brunswick, a semi-trailer manufacturer, sought to enforce a contract between its former distributor and its customer, Wisconsin Central. After Brunswick asserted that it was one of several undisclosed principals, Wisconsin Central moved for summary judgment on the grounds that the contract was unenforceable because multiple undisclosed principals existed.[13] Although the district court acknowledged that the multiple undisclosed principals argument looked promising, it held that Wisconsin Central had waived the argument by failing to plead it as an affirmative defense.[14]

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7. 152 F.3d 642 (7th Cir. 1998).
8. *Id.* at 648 n.3.
9. 151 F.3d 712 (7th Cir. 1998).
10. *Id.* at 716.
11. *Id.*
12. 136 F.3d 521 (7th Cir. 1998).
13. *See id.* at 525.
14. *See id.*

The Seventh Circuit reversed the district court's decision. At the onset, the Seventh Circuit noted that the multiple undisclosed principals rule is not one of the enumerated defenses under Federal Rule of Civil Procedure ("Rule") 8(c) and therefore must be one of the "'other' defenses" to which the rule refers.[15] After discussing the various analyses for determining whether a defense qualifies as one of the "'other' defenses" under Rule 8(c), the Seventh Circuit stated that it "need not decide which of the various analyses are 'correct,' because under any analysis the multiple undisclosed principals rule is not an affirmative defense: it is merely a part of the legal rule that permits some—but not all—undisclosed principals to enforce their agents' contracts."[16] Holding that the undisclosed principals rule completely defeated Brunswick's claims,[17] the Seventh Circuit reversed the district court's decision.

F. More Definite Statement

The decision in *In Re Rimsat, Ltd.*,[18] is an excellent example of the rare case in which a motion for a more definite statement under Rule 12 is appropriate. For those considering this procedural remedy in response to a complaint, the *Rimsat* decision is a good starting point.

G. Dismissal for Failure to Prosecute: Standards for Appointed Counsel

In *Dunphy v. McKee*,[19] the plaintiff filed a pro se civil-rights action challenging his conditions of incarceration. The district court appointed counsel to represent him, but counsel failed to prosecute the action. The district court dismissed the action for want of prosecution in a one-sentence order.[20] Plaintiff appealed, and the Seventh Circuit reversed and remanded.

The Seventh Circuit analyzed whether the standard for appointed counsel should be any different from retained counsel in this context. In the end, the court essentially followed the same standard, but noted that "[g]reater judicial oversight is . . . inevitable."[21] The court held that before dismissing an action for want of prosecution, the district court should consider four prophylactic measures: (1) the court should give due warning to counsel; (2) the court may consider giving notice to the actual plaintiff, but there is no ironclad requirement that this be done; (3) the court should analyze whether the plaintiff or counsel is at fault for the failure to prosecute; and (4) the court should consider less severe sanctions, taking into account the merits of the plaintiff's suit.[22]

Because it was unclear whether the district court had considered any of these

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15. *Id.* at 530 (quoting FED. R. CIV. P. 8(c)).
16. *Id.* (citation omitted).
17. *Id.* at 531.
18. 223 B.R. 345 (Bankr. N.D. Ind. 1998).
19. 134 F.3d 1297 (7th Cir. 1998).
20. *See id.*
21. *Id.* at 1302.
22. *Id.* at 1301.

factors, the Seventh Circuit reversed and remanded. In so doing, the Seventh Circuit suggested that the district court consider appointing substitute counsel if the dismissal were unwarranted.[23]

H. Class Actions

Rule 23 of the Federal Rules of Civil Procedure was amended by adding subdivision (f), allowing an appeal from a grant or denial of certification within ten days of the decision. The court of appeals has sole discretion whether to accept the appeal.[24]

For those defending class actions involving technical violations and modest damages, Judge Manion's decision for the Seventh Circuit in *Bailey v. Security National Servicing Corp.*,[25] could be of assistance. Judge Manion wrote:

> Class actions can benefit plaintiffs by getting a lawyer interested in taking on what individually comes close to a small claims case . . . , but litigation is costly to all concerned and uses judicial resources as well. The law[, here the Fair Debt Collection Practices Act,] would be best served by challenging clear violations rather than scanning for technical missteps that bring minimal relief to the individual debtor but a possible windfall for the attorney.[26]

II. DISCOVERY

A. Self-Critical Analysis

In *Jackson v. Preferred Technical Group Inc.*,[27] plaintiffs sought production of the employer's affirmative action plan in a race discrimination case. Defendant produced some portions of the plan, but resisted producing portions of the plan it deemed to be protected by self-critical analysis. Plaintiffs moved to compel, and Magistrate Judge Cosbey held that portions of the plan with subjective self-critical analysis were protected by the self-critical analysis privilege, while portions lacking subjective evaluative material were not privileged.[28] The opinion contains a good summary of law on the subject of self-critical analysis, and is useful for civil litigators in all contexts (not just for employment lawyers).

The key holdings of the opinion are: (a) the court recognized the self-critical analysis privilege; and (b) the court set forth the following criteria for its application: (1) whether the reports were prepared as a result of mandatory governmental requirements; (2) whether the material is subjective and evaluative

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23. *Id.* at 1302.
24. FED. R. CIV. P. 23.
25. 154 F.3d 384 (7th Cir. 1998).
26. *Id.* at 388.
27. No. 1:98-CV-21 (N.D. Ind. Oct. 21, 1998).
28. *Id.* at 5-8.

and protected or is it simply data and not protected; and (3) whether the policy favoring exclusion clearly outweighs plaintiff's need for the material.

B. Fee Agreements

In the same case, *Jackson v. Preferred Technical Group, Inc.*,[29] the defendants filed a motion to compel the disclosure of information regarding the plaintiffs' fee agreements with their counsel. The plaintiffs objected to providing such information on the grounds that it was protected from disclosure under the attorney-client privilege. The court granted the defendants' motion.[30] The court explained that "basic facts" relating to the attorney-client relationship, such as "the fact that an attorney was consulted, the nature of the services rendered by the attorney, and the details of the attorney-client fee arrangement, including the dates and amounts of payment," are not privileged.[31] The court further explained that the information was relevant to the plaintiffs' claim for attorneys' fees, and therefore discoverable.[32]

C. Medical Records

Also in the *Jackson* case, the defendants' moved to compel release of the plaintiffs' medical records. The plaintiffs objected to providing the releases based on the physician-patient privilege. The court ordered the release of the plaintiffs' medical records subject to a protective order. The court held that the plaintiffs waived the physician-patient privilege by seeking emotional damages.[33]

D. Motions to Quash from Department of Workforce Development

Local practitioners might have noticed that the Indiana Department of Workforce Development ("IDWD") is now moving to quash all subpoenas for unemployment records on the grounds that the records are confidential and cannot be disclosed without a court order. Several judges in the Southern District of Indiana have denied the IDWD's motions without even requiring a response from the defendant.[34] Until the Department alters its policy, it appears these motions to quash will continue to be filed and denied.

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29. No. 1:98-CV-21 (N.D. Ind. May 12, 1998).

30. *Id.* at 4.

31. *Id.* at 2.

32. *Id.* at 3-4.

33. No. 1:98-CV-21 (N.D. Ind. May 12, 1998) (minutes of hearing and order before Magistrate Judge Roger B. Cosbey).

34. *See, e.g.*, Ahrens v. Mead Johnson Nutritional, No. EV98-48-C-Y/H, slip. op. at 1 (S.D. Ind. June 25, 1998) (order from Magistrate Judge Hussman denying same); Skeen v. Hillhaven, No. IP98-0406-C-Y/G, slip op. at 1 (S.D. Ind. May 20, 1998) (order from Magistrate Judge Godich denying the IDWD's motion to quash subpoena and ordering the release of the requested information).

E. Discovery Responses

In *Smith v. Howe Military School*,[35] defendants' interrogatory asked whether the plaintiff had ever undergone any psychological testing or assessments, and if so, to provide details. The plaintiff answered "no." In her deposition, plaintiff testified that she had, in fact, undergone such testing.[36] Defense counsel subsequently requested supplementation, and the plaintiff's counsel responded in writing indicating some additional details of the testing but indicating that no additional information had been located.

The defendants moved to compel supplementation of the interrogatory answer. Magistrate Judge Pierce granted the motion, holding that the defendants were "entitled to receive a formal answer to the [i]nterrogatory by [the plaintiff] herself, and they are entitled to an answer under oath, not an unverified representation by her counsel."[37] The court added, "The plaintiff must respond to the interrogatory fully and completely, supplying all information within her knowledge, possession, or control, including information available through her attorneys, investigators, agents, or representatives, and any information obtainable by her through reasonable inquiry."[38]

F. Third-Party Discovery

Defendants often seek expansive third-party discovery of plaintiffs, including prior employment records, medical records, and educational records. In *Perry v. Best Lock Corp.*,[39] the defendant served nineteen non-party subpoenas upon past, present, and prospective employers of the plaintiff in an employment discrimination action. The plaintiff moved to quash the subpoenas. Judge Hamilton granted the motion, reasoning that under Federal Rule of Civil Procedure 26(b)(2) the defendant had not identified any specific concerns or targets for its "sweeping and intrusive discovery requests."[40]

III. EXPERTS

A. Daubert *Decisions*

In *Jones v. Royalton Food Service Equipment Co.*,[41] the plaintiff was injured while using a heated food cabinet, and sued the manufacturer and retailer for inadequate warnings and manufacturing defects. The defendants moved for summary judgment, and the plaintiff responded with an engineering expert to

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35. No. 3:96-CV-790RM, 1998 WL 175875 (N.D. Ind. Feb. 27, 1998).
36. *See id.* at *1.
37. *Id.* at *2.
38. *Id.*
39. No. IP98-936-C-H/G (S.D. Ind. Jan. 21, 1999).
40. *Id.* at 5.
41. No. 3:97-CV-128RP, 1998 WL 792184 (N.D. Ind. Sep. 15, 1998).

critique the dangers of the heated food cabinet.[42] The defendants moved to strike the expert's opinions as not complying with the expert witness standards of *Daubert v. Merrell Dow Pharmaceuticals, Inc.*[43]

Magistrate Judge Pierce granted the motion to strike, reasoning: (a) the expert was outside his normal field of practice such that the court was "skeptical;" (b) the expert had no special knowledge or training to conclude that the cabinet was unreasonably dangerous beyond that which would be contemplated by the ordinary consumer; (c) the expert did not consult any outside materials nor investigate any standards; and (d) the expert's opinion was "little more than subjective opinion based on a few measurements."[44] Notably, Judge Pierce also referenced that the same expert (Ned C. Myers) had been stricken by Judge Sharp in a seat-belt case.[45]

In *Ancho v. Pentek Corp.*,[46] the plaintiff was seriously injured in an industrial accident and sued the manufacturer of the equipment. The defendant moved in limine to exclude the plaintiff's design expert. The district court granted the motion and allowed the plaintiff an opportunity to name a different expert, but the plaintiff re-submitted the same expert and moved to reconsider the limine ruling.[47] Defendant then moved for summary judgment, and the court denied the motion to reconsider and granted the motion for summary judgment.[48]

On appeal, in a lengthy discussion of *Daubert* principles, the Seventh Circuit rejected the plaintiff's argument that the district court erred in excluding the design expert. Applying the deferential standard of review of manifest error for *Daubert* rulings, the Seventh Circuit held that the district judge's ruling should be affirmed.[49] Notably, even though the expert critiqued the industrial conveyor at issue, the expert had not even visited the accident site to assess the situation. The Seventh Circuit essentially held that the plaintiff had the wrong expert, writing, "[The plaintiff] should have retained a qualified plant engineer to testify at trial and his failure to do so was a mistake in judgment for which he has no one to blame but himself."[50]

B. When Does a Treating Physician Become an Expert?

In *Norwest Bank v. K-Mart Corp.*,[51] a personal injury case, the plaintiffs moved for reconsideration of Judge Miller's prior order denying their motion for leave to supplement the reports of plaintiff Deborah Frick's treating physicians.

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42. *See id.* at *3.
43. 509 U.S. 579 (1993).
44. *Jones*, 1998 WL 792184, at *6.
45. Rogers v. Ford Motor Co., 952 F. Supp. 606, 613-16 (N.D. Ind. 1997).
46. 157 F.3d 512 (7th Cir. 1998).
47. *See id.* at 514.
48. *See id.*
49. *Id.* at 518-19.
50. *Id.* at 519.
51. No. 3:94-CV-78RM (N.D. Ind. 1998).

In support of their motion, the plaintiffs stated that the opinions of Frick's treating physicians had changed since their review of information that was unavailable to them at the time of their depositions.[52] The plaintiffs claimed that Frick's treating physicians had not reviewed the information before because the plaintiffs' prior counsel was inexperienced and had failed to provide the information to Frick's treating physicians. Recognizing its significance, the plaintiffs' current counsel provided the information to Frick's treating physicians as soon as he took over the lawsuit.[53] In their motion, the plaintiffs also sought to introduce opinions from Frick's treating physicians rebutting the defendant's experts' opinions and addressing Frick's future health needs.

Noting at the outset that a treating physician can become an expert subject to the requirements of Rule 26, the court denied the plaintiffs' motion for reconsideration.[54] First, the court held that the supplemental opinions of Frick's treating physicians were subject to exclusion under Rule 37(c)(1) because the opinions were not based upon their personal knowledge and treatment of Frick.[55] The court explained:

> [T]he plaintiffs have converted Mrs. Frick's treating physicians to expert witnesses for purposes of offering new opinions based on materials provided by the plaintiffs' counsel. These supplemental opinions clearly were developed in anticipation of trial to the extent that plaintiffs' counsel chose the materials that Drs. Diamond and Elliot needed to review. . . . That Mrs. Frick's treating physicians found these additional materials beneficial to her treatment is irrelevant. Had her physicians requested these materials as essential to Mrs. Frick's care and treatment, the court may have been inclined to conclude that the supplemental opinions were not "expert" opinions for purposes of Rule 26.[56]

The court also rejected the plaintiffs' request to supplement Frick's treating physicians' opinions to rebut issues raised by the defendant's experts' reports and to address Frick's future health needs, explaining that such opinions "fall[] into the realm of expert opinion under Rule 26."[57]

Second, after concluding that the supplemental opinions of Frick's treating physicians were expert opinions, the court held that Rule 37(b)(1) required their exclusion.[58] According to the court, the opinions were not disclosed in accordance with Rule 26(a)(2)(B), there was no substantial justification for the plaintiffs' failure to disclose the opinions, and the plaintiffs' lack of compliant disclosure was not harmless.[59]

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52. *See id.* at 4.
53. *See id.*
54. *Id.* at 2-3.
55. *Id.* at 4-5.
56. *Id.*
57. *Id.* at 5.
58. *Id.* at 6.
59. *Id.* at 6-7.

IV. Summary Judgment

A. Southern District Amends Local Rule 56.1 Effective January 1, 1999

The Southern District of Indiana has been considering amendments to Southern District of Indiana Local Rule 56.1 ("Local Rule 56.1") for several years. In March 1998, the court released for public comment a proposed version of Local Rule 56.1. Written comments were invited and received from the bar, and a public hearing was held on the proposed amendments in September. As a result of that public input, the Local Rules Advisory Committee recommended certain changes to the prior proposal, and transmitted those proposals to the court for consideration. Thereafter, in November the court considered Local Rule 56.1, modified certain provisions, and passed an amendment to Local Rule 56.1 by majority vote.

B. The Key Changes

The amendment to Local Rule 56.1 makes nine key changes from current summary judgment practice, as follows:

- Timing of filings—Motions shall be filed so as to be fully briefed at least 120 days before trial unless an earlier or later deadline is provided by order or case management plan. Response briefs will be due 30 days after the motion is filed, rather than 15 days under former practice; reply briefs will be due 15 days after the response brief, rather than the former 7 days.[60]

- Extensions—As before, extensions are available under the standards of Federal Rule of Civil Procedure 6 (for "good cause"), but must now specify the trial date, any other deadline or date that might be affected by the extension, and any previous extensions obtained.[61]

- Statement of Material Facts—As under former practice, the movant must file a Statement of Material Facts, either as part of the brief or as a separate filing. The statement, however, must now consist of "concise, numbered sentences with the contents of each sentence limited as far as practicable to a single factual proposition." Each sentence must be supported by a citation to admissible evidence of record, with the citation by page and paragraph number, if possible.[62]

- Response to Statement of Material Facts—The non-movant must file

60. S.D. Ind. L.Rs. 56.1(c)-(e) (amended 1998).
61. S.D. Ind. L.R. 56.1(e) (amended 1998).
62. S.D. Ind. L.Rs. 56.1(b)(1), (f) (amended 1998).

a Response to Statement of Material Facts, which must be numbered to correspond to the sentence numbers in the movant's Statement of Material Facts. The non-movant may also submit a Statement of Additional Material Facts, which must consist of numbered sentences (starting with the next number after the last numbered sentence in the Statement of Material Facts), and citations to admissible record evidence.[63]

- Reply To Additional Material Facts—The movant may then file a Reply To Additional Material Facts, using the same numbering format described above. The movant may only supplement its prior evidence to the extent such evidence responds to the non-movant's Response to Statement of Material Facts or the non-movant's Statement of Additional Material Facts.[64]

- Surreply—In the event the moving party submits additional evidence with its reply brief or objects to evidence submitted by the non-movant, the non-movant has the right to file a surreply responding only to the moving party's new evidence and objections. Any surreply must be filed no later than 7 days after the reply brief. Otherwise no filings may be made post-reply brief without leave of court.[65]

- Effect of Filings—The court will assume that the facts claimed and supported by admissible evidence by the movant are admitted to exist without controversy except to the extent specifically controverted in the Response to Statement of Material Facts. The court will also assume that facts asserted by the non-movant are true to the extent they are supported by admissible record evidence.[66] The court may, in the interests of justice or for good cause, excuse failure to comply strictly with the terms of Local Rule 56.1.[67]

- No Proposed Findings—The amended rule no longer requires the filing of proposed findings and conclusions.

- Pro Se Notice—The amended rule delineates the notice required to be given to pro se non-movants against whom summary judgment motions are filed.[68]

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63. S.D. IND. L.RS. 56.1(c), (f) (amended 1998).
64. S.D. IND. L.R. 56.1(d) (amended 1998).
65. S.D. IND. L.R. 56.1(d) (amended 1998).
66. S.D. IND. L.R. 56.1(g) (amended 1998).
67. S.D. IND. L.R. 56.1(j) (amended 1998).
68. S.D. IND. L.R. 56.1(i) (amended 1998).

The amended rule applies to motions for summary judgment filed on or after January 1, 1999.[69]

C. Effect of Local Summary Judgment Rules

In *McGuire v. United Parcel Service*,[70] the non-moving party failed to comply with the court's local rule on summary judgment. Summary judgment was granted. On appeal, the Seventh Circuit added to the long list of cases supporting strict enforcement of summary judgment local rules. The panel wrote, "The district court strictly enforced the local rules against [the appellant], and we will do likewise."[71]

Similarly, in *Huey v. United Parcel Services, Inc.*,[72] the Seventh Circuit affirmed summary judgment for the defendant, based in part upon the plaintiff's failure to comply with the district court's local rule on summary judgment. The Seventh Circuit reaffirmed that district courts may add operational details to summary judgment practice, and that "judges need not paw over the files without assistance from the parties."[73]

D. Refinements to the Pilot Program

Several judges of the Southern District of Indiana have been testing their Pilot Program for case management and summary judgment since September 1997. During 1998 the Pilot Program was slightly refined. For those operating under a Pilot Program case (which now includes any post-September 1997 civil case assigned to Chief Judge Barker, Judge McKinney, or Judge Young (Indianapolis cases only)), a current version of the revised Pilot Program guidelines are available from the Southern District Court's webpage[74] or from the Clerk. The revised guidelines are also distributed to the plaintiff upon filing or the defendant upon removal. The most significant change to the Pilot Program is a clarification that the only jury instructions required with the case management plan are those upon which the party bears the burden of proof (e.g., for a plaintiff in an age discrimination case, the basic "elements" instruction; for a defendant in a similar case, mitigation of damages). Instructions on burden of proof, credibility, and the like are not required.

E. Decisions Under the New Pilot Program

In *Miller v. Town of Speedway*,[75] Judge McKinney quashed a plaintiff's subpoena for deposition for failure to comply with the new Pilot Program

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69. Order from the Southern District of Indiana, Dec. 17, 1998, enacting S.D. IND. L.R. 56.1.
70. 152 F.3d 673 (7th Cir. 1998).
71. *Id.* at 674.
72. 165 F.3d 1084 (7th Cir. 1999).
73. *Id.* at 1085.
74. www.insd.uscourts.gov
75. No. IP97-1707-C-M/S, slip. op. at 1, (S.D. Ind. May 12, 1998).

summary judgment procedure. In *Miller*, defendant's counsel, in accordance with the Pilot Program's guidelines, sent plaintiff's counsel a proposed statement of undisputed facts one week before the parties' joint statement of undisputed facts was required to be filed with the court. The proposed statement included an affidavit from a key witness in support of the defendant's summary judgment motion.

The parties proceeded to file their statement of undisputed facts. One week before the deadline for filing fully-briefed summary judgment motions, however, plaintiff's counsel subpoenaed the witness for deposition. Defendant's counsel moved to quash the subpoena, arguing that the Pilot Program required the parties to designate all facts relevant to any motion for summary judgment prior to filing their joint statement of disputed and undisputed facts. The defendant's counsel asserted that the plaintiff was attempting to utilize the defendant's draft of the undisputed statement of facts to serve as a roadmap for his case in violation of the Pilot Program's guidelines.[76] Judge McKinney granted the defendant's motion to quash.

F. Admissibility at Summary Judgment

The decision in *Fischer v. American Telegraph & Telephone Corp.*,[77] shows that evidence must be admissible to oppose summary judgment. The plaintiff alleged retaliation for filing a charge of discrimination. Specifically, the plaintiff alleged that she had been given a negative job reference by AT&T after leaving its employment. Her only evidence of the negative job reference was her testimony that she had been told by an unidentified secretary at Hilton Hotels that a negative job reference had been given by an AT&T vice president.[78]

The district court granted summary judgment, finding no admissible evidence of any adverse action by AT&T.[79] The Seventh Circuit affirmed, holding that the plaintiff's

> own testimony on the subject is based on the purported statement of an unidentified person in Hilton's executive office, informing [the plaintiff] that the offer of employment was revoked based on the negative reference given by [AT&T]. The substance of this conversation is inadmissible hearsay because it is an out-of-court statement "offered to prove the truth of the matter asserted."[80]

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76. See Pilot Program Guidelines stating:

> We emphasize that the court will not condone inattention to discovery which has the effect of benefitting the opponent of a motion for summary judgment. In other words, a party should not lay back and wait for the proponent's road map to be set out in a summary judgment motion and then expect to do discovery to effect a detour.

77. No. 97-2456, 1998 U.S. App. LEXIS 2810 (7th Cir. Feb. 9, 1998).
78. *Id.* at *2.
79. *Id.* at *1-2.
80. *Id.* at *5 (quoting FED. R. EVID. 801(c)).

The Seventh Circuit added, "The law is well established that 'a party may not rely upon inadmissible hearsay in an affidavit or deposition to oppose a motion for summary judgment.'"[81]

G. Contradictions at Summary Judgment

In *Sullivan v. Conway*,[82] the Seventh Circuit explained the rules at summary judgment on witnesses contradicting themselves. The court clarified that no rule exists that if there is an inconsistency in an affidavit and deposition, the deposition prevails.[83] Instead, the rule is that a prior sworn statement (written or oral) cannot ordinarily be altered later by a subsequent sworn statement (oral or written).[84] Thus, if a witness executes a sworn affidavit, she may not later create a question of fact to defeat summary judgment by contradicting that affidavit in deposition. Likewise, and in the more common situation, if the witness testifies to certain facts in her deposition, she cannot create a fact issue by submitting a contrary affidavit.

V. COSTS: PRESUMPTIONS UNDER RULE 54(D)

In *Odom v. American Art Clay Co.*,[85] the employer obtained summary judgment against the employee in her employment discrimination claim. The employer filed a bill of costs pursuant to 28 U.S.C. § 1920, seeking recovery of $1447.11 in costs. The employee plaintiff objected, asking the court to exercise its discretion not to order payment of costs because she would suffer "severe economic harm" and her lawsuit was neither frivolous nor malicious.[86]

Judge Hamilton denied the objection and granted the full costs award.[87] After noting that costs are recoverable by prevailing parties as a matter "of course" under Rule 54(d)(1), he noted that there is a "strong presumption" in the Seventh Circuit that the prevailing party will recover costs.[88] Judge Hamilton added: "Generally, only misconduct by a prevailing party worthy of a penalty or the losing party's inability to pay will suffice to justify denying costs."[89] Here, though, there was no indication of misconduct on the part of the employer, and the plaintiff failed to show that "the costs sought are beyond her ability to pay within a reasonable period of time."[90] The court concluded, "The costs awarded

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81. *Id.* at *6 (quoting Bombard v. Fort Wayne Newspapers, Inc., 92 F.3d 560, 562 (7th Cir. 1996) (citation omitted)).
82. 157 F.3d 1092 (7th Cir. 1998).
83. *Id.* at 1096.
84. *See id.*
85. No. IP97-1089-C-H/G (S.D. Ind. Feb. 11, 1999).
86. *Id.* at 1.
87. *Id.* at 2.
88. *Id.* at 1 (citing Contreras v. City of Chicago, 119 F.3d 1286, 1295 (7th Cir. 1997)).
89. *Id.*
90. *Id.* at 2.

here, it should be noted, are a minor fraction of the overall resources (including attorneys['] time and the court's time) devoted to plaintiff's lawsuit, which was without merit. If the case had been frivolous or malicious, of course, the consequences would have been quite different."[91]

VI. Sanctions

In *Fries v. Helsper*,[92] the plaintiff—in his fifth unsuccessful action against the same defendants—alleged that the defendants conspired with a Wisconsin state court judge to obtain the dismissal of his fourth lawsuit in violation of his civil rights. The defendants filed a motion to dismiss and a motion for sanctions. Judge Crabb granted the defendants' motion to dismiss.[93] The following morning, a hearing on the defendant's motion for sanctions was held. The defendants submitted affidavits documenting and explaining their fees and expenses. Neither the plaintiff nor his lawyer attended the hearing, and as a result, no objections were made to the defendants' motion.[94] Judge Crabb granted the defendants' motion, imposing almost $6000 in sanctions on the plaintiff and his lawyer for filing a frivolous lawsuit and enjoining the plaintiff from filing another lawsuit against the defendants.[95] The plaintiff appealed.

Noting that a district court's imposition of sanctions is reviewed for an abuse of discretion, the Seventh Circuit affirmed Judge Crabb's decision.[96] The Seventh Circuit held that the sanctions award, and the permanent injunction, were appropriate sanctions.[97]

VII. Appeals

A. Waiver of Arguments

In *Massachusetts Bay Insurance Co. v. Vic Koenig Leasing*,[98] the Seventh Circuit noted the general rule that "'we have no obligation to consider an issue . . . that is merely raised, but not developed, in a party's brief.'"[99] Although the Seventh Circuit proceeded to address the choice-of-law issue that was raised but not developed by the parties, it warned, "[W]e must make abundantly clear to future litigants that this case does not stand for the proposition that a choice-of-law issue will always be preserved for appellate review if or whenever the parties

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91. *Id.*
92. 146 F.3d 452 (7th Cir. 1998), *cert. denied*, 119 S. Ct. 337 (1998).
93. *See id.* at 456.
94. *See id.*
95. *See id.*
96. *Id.* at 458-59.
97. *Id.* at 459.
98. 136 F.3d 1116 (7th Cir. 1998).
99. *Id.* at 1122 (quoting Freeman United Coal Mining Co. v. Office of Workers' Compensation Programs, 957 F.2d 302, 304 (7th Cir. 1992)).

. . . cite authorities from different jurisdictions."[100]

B. *Specification in Notice of Appeal*

In *Librizzi v. Children's Memorial Medical Center*,[101] the appellee sought to dismiss the appeal asserting that the appellant's notice of appeal specified the judgment of January 1997 rather than the order of March 1997 denying reconsideration as the order under review. The Seventh Circuit denied the motion, writing:

> But this is entirely proper. It is never necessary—and may be hazardous—to specify in the notice of appeal the date of an order denying a motion under [Rules] 50 or 59. Identifying the final decision entered under Rule 58 as the "judgment, order, or part thereof appealed from" [Federal Rule of Appellate Procedure] 3(c) brings up all of the issues in the case. Pointing to either an interlocutory order or a post-judgment decision such as an order denying a motion to alert or amend the judgment is never necessary, unless the appellant wants to confine the appellate issues to those covered in a specific order. An appeal from the Rule 58 final judgment always covers the waterfront. The whole case is properly before us for decision.[102]

C. *Frivolous Appeals*

The decision in *Rumsavich v. Borislow*,[103] confirms that Seventh Circuit appeals—particularly those from bench trials—are not without risk. The appellant attempted to reverse the trial court's judgment in a bench trial that involved significant credibility issues.[104] In affirming the judgment, Judge Easterbrook wrote:

> A decision based on findings about the credibility of witnesses—as this was—is impossible to upset on appeal unless documentary or other objective evidence contradicts the credibility ruling. In this case the objective evidence strongly supports the credibility ruling. So the appeal had no hope of success—it is, in a word, frivolous.[105]

The panel proceeded to order appellant's counsel to show cause under Federal Rule of Appellate Procedure 38 as to why sanctions should not be awarded for a frivolous appeal.[106]

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100. *Id.*
101. 134 F.3d 1302 (7th Cir. 1998).
102. *Id.* at 1306 (internal citations omitted).
103. 154 F.3d 700 (7th Cir. 1998).
104. *See id.* at 702-03.
105. *Id.* at 703 (internal citations omitted).
106. *Id.* at 704.

Similarly, in *Day v. Northern Indiana Public Service Corp.*,[107] the plaintiff appealed from Judge Lozano's grant of summary judgment, which had been granted in part based on the plaintiff's failure to follow the local rule on summary judgment. On appeal, the Seventh Circuit affirmed, and imposed sanctions of $500 and a public reprimand against appellant's counsel.[108] The Seventh Circuit found such sanctions necessary because counsel had violated Circuit Rule 28(c) in his brief (requiring non-argumentative statement of facts supported by citations), and because the appeal otherwise was frivolous.[109]

D. Ineffective Assistance of Counsel in Civil Cases

In *Ellman v. Hentges*,[110] the Seventh Circuit held that "ineffective assistance of counsel, except in very limited circumstances that are not present here, cannot be grounds for reversal in a conventional civil case."[111]

VIII. MISCELLANEOUS

A. The New Judge

The Honorable Richard L. Young of Evansville has filled the vacancy left by Judge Gene Brooks' retirement. Judge Young formerly served with distinction as Judge of the Vanderburgh Circuit Court. He was born in 1953 and is a native of Iowa. He attended Drake University for his undergraduate degree, and received his law degree from George Mason University School of Law. He was admitted to practice in 1980. He is married and has two children.

Although Judge Young will be responsible for the Evansville Division, he is devoting a substantial portion of his time to the Indianapolis Division as well. Indeed, numerous pending cases from the Indianapolis Division were initially reassigned to Judge Young, and he is otherwise drawing 40% of his caseload from the Indianapolis Division.

B. Web Pages

The Southern District of Indiana has a web page with invaluable information. The web address is: *www.insd.uscourts.gov*. The most useful section of the web page allows immediate, free access to docket sheets for all cases in the Southern District. The information is current as of the previous business day. Cases can be searched by docket number or by party name. Complete docket sheets are viewable and may be printed, at your office, home, or on the road—wherever you have web access through an Internet browser.[112]

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107. 164 F.3d 382 (7th Cir. 1999).
108. *Id.* at 385.
109. *Id.* at 384-85.
110. No. 97-3595, 1998 WL 560754 (7th Cir. Sept. 1, 1998).
111. *Id.* at *3.
112. The website also provides useful information regarding the court. For instance, for the

A telephone directory for the court is also provided. Additional features include on-line access to the court's Local Rules, on-line access to the court's Attorneys' Handbook, and convenient hyperlinks to other federal resources, such as the U.S. Code, Supreme Court decisions, and the Federal Judicial Center. The court and the Clerk's office should be commended for this user friendly enhancement to serving the bar and the public. The Northern District also has a website: *www.innd.uscourts.gov.* It is not yet as complete as the Southern District's, but is undergoing enhancements during 1999.

Evansville Division, the following basic information is listed:

United States District Court
304 U.S. Courthouse
101 Northwest MLK Boulevard
Evansville, IN 47708
Phone: (812) 465-6426 FAX: (812) 465-6428
Business Hours: Monday-Friday 8:30 AM - 5:00 PM
[NOTE: Evansville, IN is on Central Standard Time (CST) and does observe Daylight Savings Time.]
Closed Sat., Sun. and Legal Holidays
Counties Served: Daviess, Dubois, Gibson, Martin, Perry, Pike, Posey, Spencer, Vanderburgh and Warrick

STATE AND FEDERAL CONSTITUTIONAL LAW DEVELOPMENTS

ROSALIE BERGER LEVINSON*

TABLE OF CONTENTS

INTRODUCTION

These materials explore state and federal constitutional law developments over the past year. The first part of this Article examines state constitutional law cases, while the remaining materials focus on state and federal court cases that raise significant and recurring federal constitutional issues.

I. DEVELOPMENTS UNDER THE STATE CONSTITUTION

Several years ago Chief Justice Randall T. Shepard invited Indiana practitioners to re-examine the state constitution as a potential source for the protection of civil liberties.[1] On the other hand, the court has emphasized that challenged statutes will be given every reasonable presumption of constitutionality and that the challenger carries a heavy burden of proof.[2] In general, the Indiana Supreme Court has explained that it will take an historical/originalist approach in interpreting the state constitution: "Questions arising under the Indiana Constitution are to be resolved by 'examining the language of the text in the context of the history surrounding its drafting and ratification, the purpose and structure of our Constitution, and case law interpreting the specific provisions.'"[3] Thus, any analysis should begin with an

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* Professor of Law, Valparaiso University School of Law. B.A., 1969, Indiana University; M.A., 1970, Indiana University; J.D., 1973, Valparaiso University.

1. Randall T. Shepard, *Second Wind for the Indiana Bill of Rights*, 22 IND. L. REV. 575 (1989).

2. *See, e.g.*, Collins v. Day, 644 N.E.2d 72, 80 (Ind. 1994) (finding that the requirement of the Privileges and Immunities Clause, article 1, section 23 of the Indiana Constitution, are independent of those imposed by the Fourteenth Amendment to the U.S. Constitution).

3. Ratliff v. Cohn, 693 N.E.2d 530, 534 (Ind. 1998) (quoting Boehm v. Town of St. John, 675 N.E.2d 318, 321 (Ind. 1996)).

examination of the text, the history from the State Constitutional Convention, as well as early decisions interpreting the state constitution.[4] As to the "purpose and structure," the court has emphasized that the drafters of the Indiana Constitution were staunch believers in Jacksonian democracy, i.e., limited government and protection of inalienable rights.[5]

In many instances this constitutional analysis may reveal that the rights protected under the state constitution are no broader than those protected under the federal constitution. For example, in *Ratliff v. Cohn*,[6] the court held that in general, article I, section 16 provides no greater protection against cruel and unusual punishment than does the Eighth Amendment, which contains the same language.[7] Similarly, in *Ajabu v. State*,[8] the Indiana Supreme Court noted that "the common interwoven history" regarding the federal and state guarantee of a privilege against self-incrimination supports the conclusion that these provisions "protect the same bundle of rights and the same constitutional values."[9] The court did caution, however, that past reliance on federal case law in construing section 14 of the state constitution "does not preclude formulation of an independent standard for analyzing state constitutional claims."[10] Based on the text, history, and case precedent the court nonetheless concluded that a murder defendant's waiver of his right against self-incrimination was knowing and voluntary even though he was unaware that an attorney retained by the defendant's father had attempted to halt police interrogation of the defendant

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4. *See id.* at 534-35.

5. *See, e.g.*, Price v. State, 622 N.E.2d 954, 962 (Ind. 1993) (arguing that populous, anti-government Jacksonian democrats triggered the constitutional revision from which our current document emerged).

6. 693 N.E.2d 530 (Ind. 1998).

7. *Id.* at 543-44. *Ratliff*, which raised several state constitutional challenges, was discussed in last year's survey Article. *See* Rosalie Berger Levinson, *State and Federal Constitutional Law Developments*, 31 IND. L. REV. 501 (1998).

8. 693 N.E.2d 921 (Ind. 1998).

9. *Id.* at 929. *See also* Carter v. State, 692 N.E.2d 464 (Ind. Ct. App. 1998) (noting that Indiana has adopted the federal *Terry* rationale in determining the legality of an investigatory stop under section 11 of the state constitution, which similarly protects against an unreasonable search or seizure). Note, however, that the Indiana Supreme Court held in *Moran v. State*, 644 N.E.2d 536 (Ind. 1994), that section 11 requires a somewhat different analysis than that used under the Fourth Amendment. Whereas the federal constitution focuses on a victim's reasonable expectations of privacy, the *Moran* court ruled that section 11 requires the focus be solely on the reasonableness of the officer's conduct. *Id.* at 540-41. Nonetheless, the court concluded in that case that a police officer's warrantless search of curbside trash was reasonable because it did not involve a trespass and it did not create a disturbance, and thus evidence seized from the search of trash containers on the streets was admissible. *Id.* at 541. *Compare* Newby v. State, 701 N.E.2d 593, 602 (Ind. Ct. App. 1998) (holding that Indiana's statutory good faith exception to the exclusionary rule, which tracks the federal rule does not violate section 11).

10. *Ajabu*, 693 N.E.2d at 929.

until he could be present.[11]

The Indiana Supreme Court has emphasized that a party wishing to rely upon the state constitution must develop a separate historical analysis. Thus, in *Valentin v. State*,[12] it reversed an appellate court decision that relied on the state double jeopardy provision because it found that the defendant's brief only invoked the federal double jeopardy clause and failed to appropriately raise and develop a separate state constitutional argument.[13] The brief did not explain why the state constitution provided protection different from that found in the federal constitution. However, the Indiana Supreme Court has been asked to grant a petition to transfer in *Richardson v. State*[14] where the defendant contended that the state double jeopardy standard is more strict than that found in the federal constitution.[15]

Further, even where the state constitution is given an independent interpretation, in many cases the end result remains the same because the state provision in reality is no more protective than the federal provision—only the analysis has changed.[16] Cases discussed in the next section illustrate this principle.

Indiana's "Equal Privileges and Immunities" Clause provides that "the General Assembly shall not grant to any citizen, or class of citizens, privileges or immunities, which, upon the same terms, shall not equally belong to all citizens."[17] In 1994, the Indiana Supreme Court in *Collins v. Day*,[18] held that federal equal protection analysis does not apply to article I, section 23 of the Indiana Constitution. Looking to the text of the provision, the expressed purpose and intent of the framers, and early decisions interpreting this section, the court concluded that section 23 requires: (1) that disparate treatment be reasonably related to inherent characteristics that distinguish the unequally treated classes, and (2) that the preferential treatment be uniformly applicable and equally available to all persons similarly situated.[19] The court emphasized, however, that substantial deference must be given to legislative judgment, which should be invalidated only "'"where the lines drawn appear arbitrarily or manifestly unreasonable.'"[20] Applying this analysis, the court sustained an Indiana statute

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11. *Id.* at 930-31.

12. 688 N.E.2d 412 (Ind. 1997).

13. *Id.* at 413. *See also* Thorpe v. State, 695 N.E.2d 967, 968 (Ind. Ct. App. 1998) (finding that defendant failed to preserve a state constitutional double jeopardy argument where he did not argue at trial or on appeal that state constitution provided different or greater protections than that found in the federal Constitution).

14. 687 N.E.2d 241 (Ind. Ct. App. 1997), *trans. pending*. *See* Jenkins v. State, 695 N.E.2d 158, 161 (Ind. Ct. App. 1998).

15. *Id.* at 242-43.

16. Moran v. State, 644 N.E.2d 536, 541 (Ind. 1994).

17. IND. CONST. art. I, § 23.

18. 644 N.E.2d 72, 80-81 (Ind. 1994).

19. *Id.* at 80.

20. *Id.* (quoting Chaffin v. Nicosia, 310 N.E.2d 867, 869 (Ind. 1974)).

that excluded agricultural employers from worker's compensation coverage because the plaintiffs could not carry their burden "to negative every reasonable basis for the classification."[21]

Most attempts by Indiana litigants to invalidate state legislative enactments under section 23 have been unsuccessful because of the highly deferential approach set forth by the Indiana Supreme Court in *Collins*. For example, in *Indiana High School Athletic Ass'n v. Carlberg*,[22] the court sustained an Indiana High School Athletic Association ("IHSAA") Transfer Rule that gives students who change residence with their parents immediate full varsity eligibility at a new school, while denying eligibility during the first 365 days following a transfer by students who move without their parents. The court emphasized that analysis under section 23 will generally be limited to determining whether a rule has a reasonable basis.[23] It found that the distinctions were reasonably related to the goal of deterring athletically motivated transfers.[24] Although conceding that some transfers might not be impermissibly motivated, the court accepted the IHSAA position that it could not afford to investigate each transfer individually.[25] Further, the harsh effect of the rule was tempered somewhat by allowing participation at the junior varsity level.[26] Thus, when examining the deterrent value of the rule, the availability of limited eligibility, and the prohibitive cost of monitoring the motives of every transfer, the court concluded that the rule was neither arbitrary nor manifestly unreasonable and thus did not violate the Privileges and Immunities Clause.[27]

In addition, the court rejected the plaintiff's claim under article I, section 12 of the Indiana Constitution, which guarantees that a remedy "by due course of law" is available to anyone "'for injury done to him in his person, property or reputation.'"[28] The court first stated that the analysis under section 12 parallels that of the federal Due Process Clause.[29] A predicate to an analysis under either provision is a determination that a claimant has a protectible property or liberty interest. The court first noted that it was unlikely that Carlberg had any protectible interest in participating in varsity athletics.[30] Further, even if such an

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21. *Id.* at 81.
22. 694 N.E.2d 222 (Ind. 1997).
23. *Id.* at 240.
24. *Id.*
25. *Id.* at 233.
26. *See id.* at 240.
27. *Id. See also* Chamberlain v. Parks, 692 N.E.2d 1380 (Ind. Ct. App. 1998) (finding that Wrongful Death Statute that allows recovery only by those financially dependent on deceased does not violate section 23 because disparate treatment is rationally related to the state's goal of assisting those financially dependent upon the deceased, and the privilege is available to all who share the inherent characteristic of financial dependency, and suffer a pecuniary loss upon the decedent's death).
28. *Carlberg*, 694 N.E.2d at 241 (quoting IND. CONST. art. I, § 12).
29. *Id.*
30. *Id.* at 241 n.26.

interest can be implied, e.g., that athletic participation may lead to athletic scholarships, the court concluded that Carlberg was not denied the procedure that he was due because the IHSAA rules provide for an appeal and Carlberg in fact was granted a hearing before the IHSAA executive committee at which he presented witnesses and exhibits.[31]

Despite this highly deferential approach under both sections 23 and 12, two appellate courts have ruled that the statute of limitations in Indiana's Medical Malpractice Act violates these provisions. In *Martin v. Richey*,[32] the plaintiffs successfully challenged the medical malpractice statute of limitations, which provides that the statute begins to run upon the occurrence of the alleged negligence rather than at the time the negligence is discovered, contrary to the general tort statute of limitations.[33] The court reasoned that the different treatment of medical malpractice victims from other tort victims who enjoy a discovery-based statute of limitations violates section 23.[34] It admitted that the scheme is "reasonably related to the goal of maintaining sufficient medical treatment and controlling malpractice insurance costs"[35] and that judges are to accord considerable deference to legislative judgments.[36] The court nonetheless concluded that injured victims who lose their claim prior to the time they even become aware of or discover the malpractice are being treated unequally: "[T]he medical malpractice statute of limitations creates an unequal burden on victims of medical negligence, thereby implicitly granting a special privilege or immunity

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31. *Id.* at 241. The court also concluded that decisions of the IHSAA constitute "state action" for purposes of federal constitutional review. *Id.* at 229. However, it determined that there is no fundamental right to participate in interscholastic sports that is entitled to heightened protection under the federal Equal Protection or Due Process Clauses. *Id.* at 242. Thus, scrutiny of IHSAA decisions under federal law will be limited to whether they have a rational basis. The court proceeded to overrule *Sturrup v. Mahan*, 305 N.E.2d 877 (Ind. 1974), which invalidated an IHSAA decision on grounds that the rule was overbroad under federal equal protection analysis. The court correctly noted that overbreadth is not part of federal equal protection analysis in the absence of a fundamental right or suspect class. *Id.* at 239. Finally, the court ruled that the IHSAA will be treated as a government agency whose decisions are subject to judicial review under the common law. *Id.* at 231. A rule or decision of the IHSAA will, however, be overruled only if it is found to be arbitrary and capricious—where it is "willful and unreasonable or without some basis which would lead a reasonable and honest person to the same conclusion." *Id.* at 233 (quoting Department of Natural Resources v. Indiana Coal Council, Inc., 542 N.E.2d 1000, 1007 (Ind. 1989)). Further, when member schools, rather than students, challenge a rule, the court will not interfere absent a showing of "fraud, other illegality, or abuse of civil or property rights having their origin elsewhere." *Id.* at 230 (citing Indiana High Sch. Athletic Ass'n v. Reyes, 694 N.E.2d 249, 256-57 (Ind. 1997)). As to the latter, it held that courts should not interfere in a school's dispute with a voluntary association of which it is a member unless it meets this higher standard. *Id.*

32. 674 N.E.2d 1015 (Ind. Ct. App. 1997), *trans. granted*, 698 N.E.2d 1192 (Ind. 1998).

33. *Id.* at 1018.

34. *Id.* at 1022.

35. *Id.*

36. *Id.* at 1021.

to victims of other torts."[37] Thus, the statute failed the second prong of *Collins*, which mandates that a classification be open to all persons who share the same inherent characteristics.[38]

As to the section 12 challenge, the court ruled that the purpose of this provision was to recognize the right of access to courts and the right to a complete tort remedy.[39] Further, section 12 emphasizes that "'[j]ustice shall be administered freely . . . completely, and without denial.'"[40] This demonstrates that the framers did not wish to confer upon the Indiana legislature any sort of broad powers, "especially not broad powers to abrogate the common law right to a remedy for tortious injuries."[41] Acknowledging the long line of cases that had previously sustained Indiana's medical malpractice law against similar constitutional challenge, the court reasoned that because of the substantial scholarly analysis that had emerged in recent years, it was not bound by these earlier decisions.[42]

A second appellate court, in *Harris v. Raymond*,[43] adopted the reasoning and holding of *Martin* as to both constitutional claims. A third court, however, rejected both rulings. In *Johnson v. Gupta*,[44] Judge Staton reasoned that there is no vested property right in a remedy for a cause of action which has not accrued until after the limitations period has passed.[45] Further, the Indiana Supreme Court previously ruled that, "the legislature has the power to modify or restrict common law rights and remedies in cases involving personal injury."[46] Because the Indiana legislature made a reasoned policy decision to ensure the availability of malpractice insurance for Indiana doctors and medical services for Indiana residents, there was no reason to abandon established precedent under section 12.[47] Further, as to the section 23 equal privileges claim, the plaintiff's status as a patient-victim and "the fact that injuries arose from a breach of duty owed by a health care provider," are distinguishing characteristics which justify disparate treatment in light of the financial uncertainties in the health care industry.[48] The court held that the second prong of *Collins* is satisfied in that all persons within the class of malpractice claimants are being treated the same. All

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37. *Id.* at 1022. Article I, section 12 requires that every person who is injured "shall have remedy by due course of law." IND. CONST. art. I, § 12.

38. *See Martin*, 647 N.E.2d at 1022.

39. *Id.* at 1024.

40. *Id.* at 1025 (quoting IND. CONST. art I, § 12).

41. *Id.*

42. *Id.* at 1026.

43. 680 N.E.2d 551 (Ind. Ct. App. 1997) (finding that occurrence-based two-year statute of limitations was unconstitutional), *trans. granted*, 698 N.E.2d 1192 (Ind. 1998).

44. 682 N.E.2d 827 (Ind. Ct. App. 1997) (finding that two-year occurrence-based statute of limitations did not violate the state constitution), *trans. granted*, 698 N.E.2d 1192 (Ind. 1998).

45. *Id.* at 830.

46. *Id.* (citing State v. Rendleman, 603 N.E.2d 1333, 1336 (Ind. 1992)).

47. *See id.*

48. *Id.* at 831.

malpractice victims have the same two years from the date of occurrence to file a claim, even though some may not discover the malpractice within this two-year period.[49]

The Indiana Supreme Court has agreed to resolve this conflict among the appellate courts and its ruling will have significant impact not only on medical malpractice statutes of limitations but on other statutes as well.[50] The Indiana Supreme Court's recent analysis in *Carlberg*[51] suggests the Court will not readily invalidate legislative judgments. The court specifically ruled in *Carlberg* that the Indiana Due Course of Law Clause provides no greater protection than the Due Process Clause of the Fourteenth Amendment, which, in general, has been used to invalidate government action only if it is arbitrary, capricious, and conscience-shocking, as will be discussed in the next section.[52] As to the section 23 analysis, the court in *Carlberg* emphasized the "substantial deference due the enactment" and the plaintiff's burden to "negative every reasonable basis" for the legislative judgment.[53] In short, the plaintiffs in *Martin* face an uphill battle.

A second area where the Indiana Supreme Court has strayed from federal constitution analysis in interpreting a parallel state provision involves free speech rights under article I, section 9 of the Indiana Constitution. That provision broadly guarantees free expression, but also provides that speakers may be held accountable "for abuse of that right."[54] In 1993, the Indiana Supreme Court in *Price v. State*,[55] held that political speech is a "core value" embodied in section 9, which the government may not materially burden.[56] It ruled that punishing political speech, even in the context of resisting arrest, is proscribed by section 9 unless the speech inflicts harm upon others "analogous to that which would sustain tort liability against the speaker."[57] Four years later, a broadcast station sought to avail itself of the *Price* analysis when it resisted a criminal defendant's request to disclose unaired video footage.[58] In *In re WTHR-TV*,[59] the station argued that gathering and disseminating information about criminal proceedings is a "core constitutional value" and that compelled disclosure of unaired video footage "materially burdens" this core value.[60]

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49. *See id.*

50. *See, e.g.*, McIntosh v. Melroe Co., 682 N.E.2d 822 (Ind. Ct. App. 1997) (presenting similar constitutional challenges under sections 12 and 23 to 10-year statute of repose in Indiana Product Liability Act), *trans. granted*, 698 N.E.2d 1193 (Ind. 1998).

51. Indiana High Sch. Athletic Ass'n v. Carlberg, 694 N.E.2d 222 (Ind. 1997). *See supra* notes 22-31 and accompanying text.

52. *Carlberg*, 694 N.E.2d at 241.

53. *Id.* at 239-40.

54. IND CONST. art. I, § 9.

55. 622 N.E.2d 954 (Ind. 1993).

56. *Id.* at 963.

57. *Id.* at 964.

58. *In re* WTHR-TV, 693 N.E.2d 1 (Ind. 1998).

59. *Id.*

60. *Id.* at 14.

The Indiana Supreme Court assumed without deciding that a material burden on newsgathering could establish a state constitutional violation.[61] It held nonetheless that the "discovery demand does not rise to the level required to establish a Section 9 violation."[62] Disclosure of the requested tape would not directly restrain any newsgathering activities: "[I]t is not reasonably apparent that requiring the press to comply with discovery requests has produced or will produce a chilling effect on the flow of information."[63] Compliance would not "amount to anything more than a slight imposition on the media, and no impairment at all of their ability to report the news."[64] Thus, litigants seeking to invoke a *Price* analysis must demonstrate both that the government is interfering with a core value and that the government's action materially burdens that value.[65] Where a core value is not implicated, the Indiana Supreme Court has adopted a mere rational basis analysis.[66]

Finally, Indiana law has differed from federal law in the area of libel. The United States Supreme Court in *New York Times v. Sullivan*[67] declared that where an elected public official sues a "citizen critic" of government for defamation, the First Amendment mandates that the official demonstrate actual malice to recover damages.[68] The Court reasoned that the "central meaning" of the First Amendment guarantees the right of citizens to criticize their government.[69] Thus, unless the government official proves that the statement was made with knowledge that it was false, or with reckless disregard of whether it was false or not, there could be no recovery.[70] The Court expanded *Sullivan* to include defamation directed at non-elected public officials[71] and private sector public figures,[72] suggesting that the content of the libel was more important than the status of the plaintiff/victim. Indeed, in a 1971 plurality opinion, the Court in

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61. *Id.* at 15.
62. *Id.* at 16.
63. *Id.*
64. *Id.*
65. Like the First Amendment, Indiana courts have ruled that section 9 applies only to government action and not that of private citizens. *See, e.g.*, Right Reason Publications v. Silva, 691 N.E.2d 1347, 1349-50 (Ind. Ct. App. 1998).
66. *See* Whittington v. State, 669 N.E.2d 1363 (Ind. 1996). Two Justices, concurring in the *Whittington* judgment, expressed concern with the court's "all or nothing" approach to section 9 analysis, i.e., political speech is "enshrined" in article I, section 9, while other forms of speech are provided little, if any, protection under a rational basis analysis. *Id.* at 1371-72 (Sullivan, J., concurring in the result; Dickson, J., dissenting and concurring in the result). Note, too, that the majority in *Whittington* narrowly construed the concept of political speech to be limited to speech which purpose is to comment on government action. *Id.* at 1370.
67. 376 U.S. 254 (1976).
68. *Id.* at 279-80.
69. *Id.* at 274-80.
70. *Id.* at 279-80.
71. *See* Rosenblatt v. Baer, 383 U.S. 75 (1966).
72. *See* Curtis Publ'g v. Butts, 388 U.S. 130 (1967).

Rosenbloom v. Metromedia, Inc.,[73] suggested that the actual malice privilege for speech would be extended to all matters of public interest.[74]

In 1974, the U.S. Supreme Court rejected the *Rosenbloom* plurality's approach, which made content of the defamation the critical factor. Instead, the Court held that because the reputational interests of private plaintiffs were weightier, such plaintiffs should be permitted to recover upon a showing of mere negligence.[75] In *Gertz v. Robert Welch, Inc.*,[76] the Court, in a 5-4 opinion, found that private plaintiffs deserved greater protection and should not be held to the actual malice standard.[77] The Court reasoned that the private figure does not voluntarily enter the vortex of public controversy or debate, like public figures or public officials.[78] Further, the private plaintiff lacks the means of self-help access to the media available to the public victim.[79] However, expressing concern for self-censorship, the Court concluded that where the speech addresses matters of public interest, states cannot apply strict liability, but instead may impose liability only where negligence is established.[80] Further, while compensatory damages may be available based on a finding of negligence, the actual malice standard must still be met to recover punitive damages.[81]

Soon after *Gertz*, an Indiana appellate court rejected the U.S. Supreme Court's approach and determined that section 9 mandated more protection for allegedly libelous material.[82] Favoring the *Rosenbloom* analysis, in *Aafco Heating & Air Conditioning Co. v. Northwest Publications*, the court held that private individuals who bring a libel action involving an event of general or public interest must prove that the defamatory falsehood was published with actual malice.[83] In 1990, another Indiana appellate court panel reiterated the rule that section 9 requires that interchange of ideas on all matters of public or general interest be unimpaired.[84] In short, section 9 creates a constitutional privilege

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73. 403 U.S. 29 (1971).

74. *Id.* at 52.

75. *See* Gertz v. Robert Welch, Inc., 418 U.S. 323 (1974).

76. *Id.*

77. *Id.* at 343-44.

78. *Id.* at 344-45.

79. *See id.* at 344.

80. *Id.* at 346-48.

81. *Id.* at 349-50.

82. *See* Aafco Heating & Air Conditioning Co. v. Northwest Publications, Inc., 321 N.E.2d 580 (Ind. App. 1974).

83. *Id.* at 586.

84. *See* Near Eastside Community Org. v. Hair, 555 N.E.2d 1324 (Ind. Ct. App. 1990); *see also* Chang v. Michiana Telecasting Corp., 900 F.2d 1085, 1087 (7th Cir. 1990) ("No Indiana court has disagreed with *Aafco*, and four years ago we took *Aafco* to be the established law in Indiana."); Moore v. University of Notre Dame, 968 F. Supp. 1330 (N.D. Ind. 1997) (holding that because Indiana law provides that a private individual may recover for injury caused by defamation only if he can prove the publication was made with actual malice, it is unnecessary to determine whether former offensive line football coach at a university was a public figure or private individual; further,

regarding publication of all matters of general concern, regardless of whether the defamed party is a private or public individual.

Following this well-established case precedent, the Indiana Court of Appeals in *Journal-Gazette Co. v. Bandido's, Inc.*,[85] applied the actual malice standard and rejected a libel claim against a newspaper that allegedly "defamed" Bandido's restaurant by suggesting that rats had been discovered at its establishment in Indianapolis.[86] At trial, the jury had awarded significant damages ($985,000), but the appellate court determined that the record would not support a finding of actual malice.[87] The sub-heading in an article that described closing the restaurant by the health board erroneously used the word "rat" instead of rodent. The Court of Appeals held that "[e]vidence of an extreme departure from professional journalistic standards, without more, cannot provide a sufficient basis for finding actual malice."[88] The court reasoned that,

> while the Journal may well have been extremely careless in printing the subheadline with the word "rats," there is not sufficient clear and convincing evidence to demonstrate that the paper had knowledge that the headline was false or that the paper entertained serious doubts as to the truth of the headline.[89]

Although the evidence suggested that the newspaper fell below reasonable journalistic standards, and violated its own policy, this alone does not constitute actual malice.[90] The Indiana Supreme Court, which has never ruled on the issue, has granted transfer to determine whether Indiana should join the vast majority of states who utilize a negligence standard, rather than an actual malice standard, when the victim of libelous material is a private individual.[91]

II. Federal Constitutional Law

A. Federalism

One of the most significant trends in the Supreme Court is its growing sensitivity to federalism, i.e., the need to maintain a proper balance between state

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coach failed to establish actual malice on the part of the defendants as required to establish liability).

85. 672 N.E.2d 969 (Ind. Ct. App. 1996), *trans. granted*, 690 N.E.2d 1183 (Ind. 1997).

86. *Id.* at 972.

87. *Id.*

88. *Id.* (citing Harte-Hanks Communications, Inc. v. Connaughton, 491 U.S. 657, 665 (1989)).

89. *Id.* at 973.

90. *See id.*

91. Other than Indiana, only Alaska, Colorado and New Jersey still use the "actual malice" standard for private victims of libel. *See* Gay v. Williams, 486 F. Supp. 12, 15 (D. Alaska 1979); Diversified Management v. Denver Post, 653 P.2d 1103, 1106 (Colo. 1982); Sisler v. Gannett Co., 516 A.2d 1083, 1095 (N.J. 1986), *aff'd on reh'g*, 536 A.2d 299 (N.J. Super. Ct. App. Div. 1987).

and federal power. The concern for states' rights, as embodied in the Tenth and Eleventh Amendments to the Constitution, is reflected in several recent decisions addressing Congress' power under the Commerce Clause. In *Printz v. United States*,[92] the Court held that Congress exceeded its power in passing the Brady Handgun Act, which commanded the states' chief law enforcement officers to search records to ascertain whether a person could lawfully purchase a handgun. The Court reasoned that the history and structure of the Constitution prohibit Congress from compelling state executive officers to enforce a federal regulatory program.[93]

In *United States v. Lopez*,[94] it ruled that Congress exceeded its power in passing a federal criminal statute prohibiting the possession of a firearm within 1000 feet of a school. Congress had not made clear findings demonstrating that the regulated activity substantially affected interstate commerce.[95] Additionally, the Court stressed that the criminal statute had nothing to do with commerce, nor was possession of firearms in any way connected with a commercial transaction.[96] Further, the statute lacked a jurisdictional element that would require prosecutors to demonstrate a link to commerce on a case-by-case basis,[97] and the statute governed areas historically left to states, namely criminal law enforcement and education.[98]

The concern for states' rights is also apparent in a series of decisions invoking the states' Eleventh Amendment protection from suit in federal court. In *Seminole Tribe of Florida v. Florida*,[99] the Supreme Court held that Congress lacks the power to abrogate the Eleventh Amendment when it acts under the Commerce Clause, and thus Florida could not be subjected to suit in federal court.[100] In *Idaho v. Coeur d'Alene Tribe of Idaho*,[101] the Court held that a federal court may not hear an action against state officers for injunctive and declaratory relief when such relief requires adjudication of a state's title and will deprive the state of all practical benefits of ownership of disputed waters and submerged lands.[102] This was the first time since 1908 that the Supreme Court disallowed a suit for injunctive relief as opposed to damages against a state entity in a federal court.[103]

In addition, the Supreme Court has questioned Congress' power to limit state sovereignty even when it invokes section 5 of the Fourteenth Amendment, which

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92. 117 S. Ct. 2365 (1997).
93. *Id.* at 2369-84.
94. 514 U.S. 549 (1995).
95. *See id.* at 562-63.
96. *Id.* at 561.
97. *See id.* at 562.
98. *See id.* at 564.
99. 517 U.S. 44 (1996).
100. *Id.* at 72-73.
101. 521 U.S. 261 (1997).
102. *Id.* at 287-88.
103. *Id.* at 266.

allows Congress to enact legislation to enforce the Equal Protection and Due Process Clauses.[104] Unlike the Commerce Clause, this amendment was intended to alter the balance of power and restrict state authority.[105] Nonetheless, the Supreme Court in *City of Boerne v. Flores*,[106] held that Congress had exceeded its power. In *City of Boerne* the Supreme Court struck down the Religious Freedom Restoration Act of 1993 ("RFRA"),[107] reasoning that Congress went beyond merely enforcing the substantive right to religious liberty guaranteed by the Fourteenth Amendment; rather, Congress had created new substantive rights.[108] Although in part the Court obviously was flexing its judicial muscle as the branch of government with final authority to interpret the Constitution, it also opined that Congress had violated state sovereignty by requiring states to justify by an overriding interest any law that had an adverse impact on some religious practice.[109]

The ramifications of these decisions is clearly being felt in the lower courts. In *Mueller v. Thompson*,[110] the Seventh Circuit joined the First, Fourth, Sixth, Eighth, and Tenth Circuits in holding that the Eleventh Amendment bars suits against a state employer in federal court under the Fair Labor Standards Act ("FLSA"), which was enacted under Congress' power to regulate interstate commerce.[111] The court in *Mueller* further ruled that the State of Wisconsin did not waive this immunity by enacting legislation authorizing suits against state employers under state statutes addressing overtime pay.[112] The court noted that after *Seminole Tribe* "states will have to decide whether they want to allow

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104. Section 5 of the Fourteenth Amendment provides that Congress shall have the power to enforce the guarantees of the Fourteenth Amendment "by appropriate legislation." U.S. CONST. amend. XIV, § 5.

105. The Supreme Court ruled in the 1960s that section 5 is "a positive grant of legislative power authorizing Congress to exercise its discretion in determining whether and what legislation is needed to secure the guarantees of the Fourteenth Amendment." Katzenbach v. Morgan, 384 U.S. 641, 651 (1966). Chief Justice Rehnquist wrote in a 1976 decision that the principle of state sovereignty is

> necessarily limited by the enforcement provisions of § 5 of the Fourteenth Amendment .... When Congress acts pursuant to § 5, not only is it exercising legislative authority that is plenary within the terms of the constitutional grant, it is exercising that authority under one section of a constitutional Amendment whose other sections by their own terms embody limitations on state authority.

Fitzpatrick v. Bitzer, 427 U.S. 445, 456 (1976). Justice Rehnquist cited the Fourteenth Amendment and observed that it "quite clearly contemplates limitations on [state] authority" and represents a "shift in the federal-state balance." *Id.* at 453-55.

106. 117 S. Ct. 2157 (1997).

107. 42 U.S.C. §§ 2000bb1-2000bb4 (1994).

108. For a discussion of RFRA, see *infra* notes 366-85 and accompanying text.

109. *City of Boerne*, 117 S. Ct. at 2169-71.

110. 133 F.3d 1063 (7th Cir. 1998).

111. *Id.* at 1064-66. *See* 29 U.S.C. §§ 201-19 (1994 & Supp. II 1996).

112. *Mueller*, 133 F.3d at 1064-65.

FLSA suits to be brought in federal as well as state court against them."[113] However, any waiver must be clear.

Thus far the state courts have also split on whether they must make their own courts available to hear these claims. The Maine Supreme Court has held that Congress cannot force state courts to entertain FLSA claims, thus in essence nullifying FLSA as to state employers.[114] However, the Arkansas Supreme Court has ruled that Congress exercising its Commerce Clause power may subject an unconsenting state to suit for monetary relief in its own state courts even when it cannot validly subject the state to such suit in a federal forum.[115] The Supreme Court will review this question during the 1998-99 Term.[116]

In *Velasquez v. Frapwell*,[117] the Seventh Circuit held that Indiana University, a state employer, could not be sued in federal court under the Uniformed Services Employment and Reemployment Rights Act ("USERRA"),[118] which prohibits discrimination in employment against members of the armed forces and authorizes private suits for damages and injunctive relief against the employer—including a state employer. The court initially found that Congress was exercising its war powers under Article I when it enacted this provision.[119] Relying on *Seminole Tribe*, the court reasoned that when Congress exercises power under any provision of Article I, it may not abrogate the states' Eleventh Amendment immunity.[120]

In addition, the court concluded that Congress could not be deemed to have enacted USERRA under section 5 of the Fourteenth Amendment and that, even if Congress had explicitly relied on section 5, its attempt to do so would be barred by the Supreme Court's decision in *City of Boerne*.[121] The authorization in this federal statute for private lawsuits in federal court against state employers could not be sustained as an exercise of congressional power under the Fourteenth Amendment, which must be adapted to remedying wrongs targeted by that Amendment. The statute's main purpose was to encourage people to join the armed forces reserves, not to combat any invidious discrimination against members of the armed services.[122] This was "at most a distinctly secondary purpose of [USERRA]," too remote from the policies and objectives of the Equal Protection Clause to invoke section 5.[123] Thus, this lawsuit could not be maintained in federal court against Indiana University, an instrumentality of the

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113. *Id.* at 1066.

114. Alden v. Maine, 715 A.2d 172 (Me.), *cert. granted* 119 S. Ct. 443 (1998).

115. Arkansas Dep't of Educ. v. Jacoby, 962 S.W.2d 773 (Ark. 1998), *request for cert. pend'g.*

116. Alden v. Maine, 715 A.2d 172 (Me.), *cert. granted*, 119 S. Ct. 443 (1998).

117. 160 F.3d 389 (7th Cir. 1998), *vacated in part*, 165 F.3d 593 (7th Cir. 1999).

118. 38 U.S.C. §§ 4301-33 (1994 & Supp. II 1995).

119. *Velasquez*, 160 F.3d at 392.

120. *Id.* at 393.

121. *Id.* at 391.

122. *See id.* at 392.

123. *Id.*

state, because of the Eleventh Amendment barrier.[124] The court later learned that on the day before it rendered its opinion, Congress amended USERRA to confer jurisdiction only on state courts over suits against a state employer.[125] As a result, the court vacated its opinion and reaffirmed dismissal on grounds that it lacked jurisdiction over the USERRA claim.[126]

The state sovereignty defense did not fare as well in other cases. For example, the Seventh Circuit in *United States v. Black*,[127] ruled that the Child Support Recovery Act ("CSRA"),[128] which regulates non-payment of interstate child support obligations, was a valid exercise of Congress' power under the Commerce Clause. Distinguishing *Lopez*, the court reasoned that the CSRA addresses only non-payment of interstate child support obligations and thus it regulates something in interstate commerce: "[A] parent's intentional failure to pay child support constitutes a conscious impediment to interstate commerce that Congress can criminalize."[129] Further, the legislative history addressed the problem of interstate enforcement of child support and the bill was designed solely to target interstate cases: "Congress made express findings that collecting child support from out-of-state parents has grown beyond the States' enforcement capabilities."[130] Because this was a valid exercise of Congress' power, the court also rejected the purported Tenth Amendment claim that the CSRA violated the states' traditional authority over matters concerning domestic relations and enforcement of criminal laws.[131]

Similarly, in *Travis v. Reno*,[132] the Seventh Circuit sustained the federal Driver's Privacy Protection Act (the "Act"), which restricts the disclosure of personal information that states maintain in drivers' records.[133] The district court had ruled that the Act violated the Tenth Amendment because it required the states to administer and enforce a detailed federal program.[134] Although conceding that the Act would force states to alter the way they handled requests for information, the appellate court reasoned that the Act affected states only as owners of data, not as sovereigns. Recognizing that numerous federal statutes impose record-keeping requirements on state government, the court explained that "the anti-commandeering rule comes into play only when the federal government calls on the states to use their sovereign powers as regulators of their citizens."[135] It rejected the Fourth Circuit's broader interpretation of *Printz* that

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124. *See id.*
125. 165 F.3d 593 (7th Cir. 1999).
126. *See id.* at 594.
127. 125 F.3d 454 (7th Cir. 1997).
128. 18 U.S.C. § 228 (1994 & Supp. III 1997).
129. *Black*, 125 F.3d at 460.
130. *Id.* at 462.
131. *Id.* at 462-63.
132. 163 F.3d 1000 (7th Cir. 1998).
133. *See* 18 U.S.C. §§ 2721-25 (1994 & Supp. III 1997).
134. 12 F. Supp. 2d 921 (W.D. Wis. 1998).
135. *Travis*, 163 F.3d at 1004-05.

would restrict Congress to regulating states only through laws of general applicability.[136]

Similarly, in *Gillispie v. City of Indianapolis*,[137] the district court rejected state sovereignty claims and sustained the Lautenberg Amendment to the Gun Control Act of 1968,[138] which prohibits a person who has been convicted in any court of a misdemeanor claim of domestic violence from owning a firearm. The Lautenberg Amendment applies to law enforcement officers and it was invoked by the Indianapolis Police Department to terminate a police officer who pled guilty to a misdemeanor battery offense involving his ex-wife. The court ruled that this section does not invade state sovereignty in violation of the Tenth Amendment.[139] It has only an ancillary effect on the employment of state and local law enforcement officers and it does not force states to administer and enforce a federal regulatory program, as was the case in *Printz*.[140] Further, the amendment was held to be a proper exercise of Congress' power under the Commerce Clause because, unlike the statute in *Printz*, the law contained an express requirement that the prosecution prove the firearm in question was shipped or transported in interstate commerce.[141] This "jurisdictional nexus" defeats the Commerce Clause challenge.[142]

The Seventh Circuit also overrode Eleventh Amendment state sovereignty defenses by invoking the congressional abrogation doctrine. In *Goshtasby v. Board of Trustees*,[143] the court held that Congress validly exercised its power under section 5 of the Fourteenth Amendment in applying the Age Discrimination in Employment Act ("ADEA")[144] to state employers. The court reasoned that the 1974 amendment to the ADEA's definition of employer to include state and local government was a clear expression of Congress' intent to override state sovereignty.[145] Further, although Congress did not state explicitly that it was acting under section 5 when it amended the ADEA, the court ruled that the legislature need not recite the constitutional basis for its enactment in order to effect a valid exercise of power.[146] Distinguishing *City of Boerne*, the court reasoned that RFRA was a statute "'so out of proportion to the problems

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136. *Id.* at 1006. In *Condon v. Reno*, 155 F.3d 453 (4th Cir. 1998), the Fourth Circuit held this Act exceeded Congress' authority under the Commerce Clause.

137. 13 F. Supp. 2d 811 (S.D. Ind. 1998).

138. 18 U.S.C. § 922(g)(9) (1994).

139. *Gillispie*, 13 F. Supp. 2d at 819-21.

140. *Id.* at 820.

141. *Id.* at 822.

142. *See id. Compare* Fraternal Order of Police v. United States, 152 F.3d 998 (D.C. Cir.), *reh'g granted*, 159 F.3d 1362 (D.C. Cir. 1998) (holding that this statute violates the Equal Protection Clause because it imposes a federal firearms disability on persons convicted of domestic misdemeanors, but not domestic violence felonies—a distinction without any rational justification).

143. 141 F.3d 761 (7th Cir. 1998).

144. 29 U.S.C. §§ 621-34 (1994 & Supp. III 1997).

145. *Goshtasby*, 141 F.3d at 766.

146. *Id.* at 768.

which it identified that the Act could not be viewed as enforcing the provisions of the Fourteenth Amendment.'"[147] In contrast, the ADEA is not out of proportion to the problem that it addresses—the act is supported by legislative findings of intentional discrimination against workers because of their age. The court explained that "[t]he critical question remains whether the act remedies constitutional violations or whether it imposes new substantive constitutional rights through legislation."[148] The ADEA falls within the former category. Finally, the fact that age is not a "suspect classification" does not foreclose Congress from enforcing the Equal Protection Clause through a statute that protects against arbitrary and invidious age discrimination.[149] On the other hand, the Eighth and Eleventh Circuits have ruled that because Congress did not clearly express its intent to abrogate immunity in enacting the ADEA, state employers may not be sued in federal court.[150] The Supreme Court will resolve the circuit dispute during the 1998-99 Term.[151]

The Seventh Circuit followed the *Goshtasby* analysis in *Varner v. Illinois State University*,[152] holding that "magic words" are unnecessary where the intent to abrogate is clear.[153] Thus, the 1974 amendments to the Fair Labor Standards Act, which authorized employees to sue public agencies in federal court for Equal Pay Act ("EPA") violations, sufficiently demonstrates intent to abrogate state immunity.[154] The court rejected the state university's argument that the legislative history demonstrated Congress' reliance on the Commerce Clause, rather than section 5 of the Fourteenth Amendment; instead it found the legislative history to be "murky."[155] As to the *City of Boerne* question, the court ruled that the purpose of the EPA was to prohibit arbitrary, discriminatory government conduct, and thus it is a valid exercise of congressional power to enforce the equal protection guarantee of the Fourteenth Amendment.[156] In the

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147. *Id.* at 769 (quoting City of Boerne v. Flores, 117 S. Ct. 2157, 2170 (1997)).

148. *Id.*

149. *See id.* at 770. *Accord* Keeton v. University of Nev. Sys., 150 F.3d 1055, 1057 (9th Cir. 1998) (citing cases from several circuits reaching this same conclusion).

150. Kimel v. State of Fla. Bd. of Regents, 139 F.3d 1426 (11th Cir. 1998) (finding that because there is no unequivocal expression of an intent to abrogate immunity in the ADEA, nor is there a plain statement that state employers may be sued in federal court under this provision, states may not be sued by private citizens in federal court for age discrimination), *cert. granted*, 119 S. Ct. 901 (1999)); Humenansky v. Regents of the Univ. of Minn., 152 F.3d 822 (8th Cir. 1998) (holding that ADEA amendments did not clearly indicate Congress' intent to abrogate and they were not enacted pursuant to the Fourteenth Amendment).

151. *See Kimel*, 119 S. Ct. at 901 (granting cert.).

152. 150 F.3d 706 (7th Cir. 1998).

153. *Id.* at 712-13.

154. *Id.* at 710.

155. *Id.* at 714.

156. *Id.* at 714-17. Although the EPA reaches gender-based wage disparity even where such is unintentional, whereas the Equal Protection Clause has been interpreted to require proof of discriminatory intent, this does not indicate that the EPA is substantive legislation beyond the scope

same vein, the Seventh Circuit has determined that the Americans with Disabilities Act ("ADA")[157] was lawfully enacted under section 5 of the Fourteenth Amendment and, therefore, abrogates any Eleventh Amendment defense to suit in federal court.[158]

B. Procedural and Substantive Due Process

As in past years, several litigants claimed their procedural due process rights were violated. The Supreme Court applies a two-prong analysis, requiring that a plaintiff initially identify a property or liberty interest. Assuming this burden is met, the Court then balances the competing interests to determine whether sufficient procedural safeguards have been afforded. As to the latter step, the Court balances (a) the private interest affected; (b) the risk of erroneous deprivation and the value of additional procedural safeguards; and (c) the government's interests.[159]

In *Family & Social Services Administration v. Jones*,[160] the court ruled that a licensed childcare provider had a property interest in a childcare license because the statutory qualifications were objective, leaving little discretion to the issuing agency. The holder had a legitimate claim of entitlement and, therefore, a property interest in the license.[161] Further, the court ruled that the administrative hearing held in connection with the proceeding to suspend the license, during which the provider was not given the opportunity to challenge the underlying allegations of abuse, did not comport with due process.[162] The court reasoned that the administrative law judge essentially ignored any evidence which tended to show that the allegations of abuse had not occurred.[163]

Similarly in *Alston v. King*[164] the Seventh Circuit upheld the district court's

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of section 5 enforcement powers. *City of Boerne* itself recognized that section 5 remedial legislation may prohibit conduct that is not itself unconstitutional if there is "a congruence and proportionality between the injury to be prevented or remedied and the means adopted to that end." City of Boerne v. Flores, 117 S. Ct. 2157, 2159 (1997). In *Varner*, significant congressional findings demonstrated that pervasive wage discrimination existed between men and women, and the EPA was reasonably tailored to remedy that problem. *Varner*, 150 F.3d at 716. *Accord* Ussery v. Louisiana, 150 F.3d 431, 435 (5th Cir. 1998) (citing cases from several circuits finding that Congress clearly stated in the EPA its intent to abrogate the states' Eleventh Amendment immunity), *cert. denied*, 119 S. Ct. 1161 (1999).

157. 42 U.S.C. §§ 225, 12101-213 (1994 & Supp. II 1996).

158. Crawford v. Indiana Dep't of Corrections, 115 F.3d 481 (7th Cir. 1997). *Accord* Autio v. AFSCME, Local 3139, 157 F.3d 1141 (8th Cir. 1998); Clark v. California, 123 F.3d 1267 (9th Cir. 1997).

159. *See* Mathews v. Eldridge, 424 U.S. 319, 334-35 (1976).

160. 691 N.E.2d 1354 (Ind. Ct. App. 1998).

161. *Id.* at 1356.

162. *Id.* at 1357.

163. *Id.*

164. 157 F.3d 1113 (7th Cir. 1998).

ruling that termination of a city employee without a meaningful pretermination hearing violates due process.[165] Although the City argued that the employee's threats to shut off the water supply to City Hall justified immediate action, the district court properly determined that "the City's asserted interest could have been accomplished through suspension rather than termination."[166] A suspension, rather than the ultimate sanction of termination, was constitutionally required until the employee was afforded a hearing.[167]

Most Indiana litigants, however, did not fare as well in bringing their procedural due process cases. Some failed to meet the threshold question of establishing a property interest. In *Moulton v. Vigo County*,[168] Moulton claimed he had a protected property interest in his job at the county area plan department. The court examined Indiana Code section 36-7-4-312(5) and concluded that it "did not specify a term of employment for employees of the Plan department, nor [did] it establish that employees could be removed only for cause."[169] The county's policy of giving plan commission members a pre-termination hearing did not establish that the plaintiff had a property right in his job, and there was no evidence in the record demonstrating that the commission promulgated any county termination policies.[170]

In other cases, a protected property interest was found, but the court determined that the procedural safeguards were adequate. For example, in *Tweedal v. Fritz*,[171] the court rejected procedural due process claims brought by a teacher suspended from school and allegedly constructively discharged for making inappropriate sexual comments to a student. The teacher was initially suspended with pay until a hearing could be held, where he was given an opportunity to respond to his accusers.[172] Although conceding that the teacher's interest in protecting his reputation was substantial, the court noted that "the government's interest in protecting children from a teacher's sexual misconduct is urgent and extreme."[173] Further, the suspension with pay was based on

165. *Id.* at 1117.

166. *Id.* ("in those situations where the employer perceives a significant hazard in keeping the employee on the job, it can avoid the problem by suspending with pay") (citing Cleveland Bd. of Educ. v. Loudermill, 470 U.S. 532, 544-45 (1985)). *See also* Staples v. City of Milwaukee, 142 F.3d 383, 386 (7th Cir. 1998) (holding that contemporaneous rather than advance notice given during a hearing convened for an entirely different purpose fails to satisfy *Loudermill*).

167. *See Alston*, 157 F.3d at 1117. On the other hand, the court ruled that the jury was improperly instructed that it could award damages for the termination rather than for the consequences of being denied a hearing before termination, and thus the award of damages was reversed. *Id.* at 1118.

168. 150 F.3d 801 (7th Cir. 1998).

169. *Id.* at 805.

170. *Id.*

171. 987 F. Supp. 1126 (S.D. Ind. 1997).

172. *Id.* at 1128.

173. *Id.* at 1133.

credible accusations and carried with it a low risk of erroneous deprivation.[174] In addition, post-deprivation remedies, which fully comported with due process standards, were available within a week after the suspension.[175]

In *Gagne v. Trustees of Indiana*,[176] a former law student sought judicial review of an administrative determination expelling him from the state university's law school. The court held that the procedure used to determine appropriate discipline for the student did not violate his due process rights. The student, who was accused of violating the Code of Ethics, received all the process that he was due—notice, a hearing, and an opportunity to respond, explain, and defend.[177] Although the court noted that due process requires that the university base an expulsion on substantial evidence, the court also found that the university was not required to follow the same legal formalities as state-wide administrative bodies in taking evidence.[178] The court ruled that for school expulsion, due process requires only an informal give-and-take between the student and the disciplinarian, where the student is given an opportunity to explain his version of the facts.[179] Gagne was given that opportunity and in fact, his attorney made opening and closing statements and presented witnesses on Gagne's behalf, and Gagne also spoke at length explaining his reasons for enclosing false statements on his application for admission and resume for employment.[180]

The U.S. Supreme Court has recognized that the Due Process Clause[181] also contains a substantive component that bars arbitrary, wrongful conduct. Where the government interferes with a fundamental right, the Court has demanded that the conduct meet a strict scrutiny standard. The government action must be narrowly tailored to support a compelling interest. Where no fundamental right is identified, however, the Court generally has been very reluctant to find a substantive due process violation, requiring the plaintiff to demonstrate that the government has acted in a truly "conscience-shocking" fashion before it will intervene.

This all-or-nothing approach to substantive due process was questioned in

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174. *Id.* at 1132. The court relied on the Supreme Court's decision in *Gilbert v. Homar*, 117 S. Ct. 1807 (1997), sustaining immediate suspension of a university police officer following his arrest on drug-related charges, despite early precedent suggesting that some minimal pre-deprivation process, i.e., notice and an opportunity to respond, is normally required in the employment context. *Tweedal*, 987 F.Supp. at 1133-34.

175. *Id.* at 1133.

176. 692 N.E.2d 489 (Ind. Ct. App. 1998).

177. *See id.* at 493.

178. *Id.* at 493-94.

179. *Id.* at 493.

180. *Id.* at 493-94. *See also* Zimmerman v. Tippecanoe Sheriff's Dep't, 25 F. Supp. 2d 915 (N.D. Ind. 1998) (finding that inmate who claimed defendant removed material from his incoming mail could not pursue procedural due process claim because Indiana law provides an adequate remedy for deprivation of property by municipal officials).

181. U.S. CONST. amend. XIV.

Sightes v. Barker.[182] A grandmother, who was the mother of a child's biological father, petitioned to establish visitation under Indiana's Grandparent Visitation Act.[183] The mother and her new husband moved to dismiss the petition, alleging the state statute unconstitutionally burdened their autonomous right as parents to raise their child. While recognizing the fundamentality of parental rights, the court noted that "family autonomy is not absolute" and that the degree of the alleged infringement must be examined to determine the constitutionality of the statute.[184] The court reasoned that allowing grandparent visitation over parents' objection did not unconstitutionally impinge upon the integrity of the adoptive family because visitation could only be granted following the filing of a verified petition, a hearing, and an entry of a decree supported by findings that this would best serve the interests of the child.[185] Further, the court noted that even if strict scrutiny was applied, the state had a compelling interest in protecting the best interests of the child and in maintaining the right of association of grandparents and their grandchildren.[186]

Associational rights have also been raised by defendants challenging Illinois' loitering ordinance. The Supreme Court has agreed to review the constitutionality of a Chicago ordinance that authorizes the arrest of persons who have disobeyed a police order to move on, when the officer has reasonable cause to believe that the group of loiterers includes a member of a criminal street gang. In *City of Chicago v. Morales*,[187] the Illinois Supreme Court found that the ordinance unreasonably infringed upon the personal liberty of being able to freely walk streets and associate with others and, therefore, violated substantive due process.[188]

In general, the United States Supreme Court has shown a great reluctance to intervene under the somewhat amorphous substantive due process provision, or to find that the conduct of government officials meets the stringent conscience-shocking standard. The Court has frequently voiced concern for constitutionalizing everyday torts, which should be left to state law.[189] Indeed the only area where the conscience of the Justices appears to have been "shocked" is in the area of excessive punitive damage awards. In *BMW of North America,*

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182. 684 N.E.2d 224 (Ind. Ct. App. 1997).
183. IND. CODE §§ 31-17-5-1 to -10 (1998).
184. *Sightes*, 684 N.E.2d at 229.
185. *Id.* at 230-31.
186. *Id.* at 233.
187. 687 N.E.2d 53 (Ill.), *cert. granted*, 118 S. Ct. 1510 (1998).
188. *Id.* at 65. *Compare* Klein v. State, 698 N.E.2d 296 (Ind. 1998) (upholding Indiana's Criminal Gang Activity statute, which defines a criminal gang as a group that promotes, sponsors, assists in, or participates in a felony. The law was not unconstitutionally vague or overbroad, even as amended to exclude a previous requirement that the gang mandate commission of a felony as a condition of membership. The statute did not criminalize mere status of gang membership, but applied only to criminal associations that are not protected by the First Amendment.).
189. *See* Paul v. Davis, 424 U.S. 693, 699 (1976).

Inc. v. Gore,[190] the Supreme Court held that a $2 million punitive damages award was grossly excessive and exceeded constitutional limits.[191] The Court outlined three criteria that should be examined in determining whether punitive damage awards should be deemed excessive: (1) the reprehensibility of the conduct, in particular whether only economic harm is involved; (2) the relation between compensatory and punitive damages; and (3) the relation of the damages to other civil remedies authorized or imposed in comparable cases.[192] Both federal and state courts in Indiana appear to be applying the *BMW* factors in assessing constitutional challenges to punitive damage awards.[193]

Outside the area of punitive damages, litigants face an uphill battle in establishing a substantive due process violation. In *County of Sacramento v. Lewis*,[194] the Supreme Court reviewed the conduct of a deputy sheriff who conducted a high-speed chase of two boys on a motorcycle when they failed to obey another officer's command to stop. In violation of departmental policy, the deputy continued the pursuit at speeds of up to 100 miles-per-hour in a residential area. The chase ended seventy-five seconds after it began when the motorcycle overturned and the deputy's vehicle skidded into the boy who was riding on the back of the motorcycle, killing him.[195]

Addressing the substantive due process standard, the Supreme Court noted that "the cognizable level of abuse of executive power [is] that which shocks the conscience."[196] The Ninth Circuit held that the deputy had acted with deliberate indifference to the boys' safety and thus his conduct met the "shocks the conscience" standard.[197] Reversing the appellate court, the Supreme Court reasoned that "[d]eliberate indifference that shocks in one environment may not be so patently egregious in another . . . ."[198] Thus, while the Court in *Revere*

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190. 517 U.S. 559 (1996).

191. *Id.* at 585.

192. *Id.* at 574-75.

193. *See* Michigan Mut. Ins. Co. v. Sports, Inc., 698 N.E.2d 834 (Ind. Ct. App. 1998) (finding that punitive damages award of $1 million against a property insurer for bad faith denial of coverage for a fire loss was not so excessive as to violate due process; although award was nearly fourteen times greater than compensatory damages award, insurer acted intentionally and left purchaser financially vulnerable to both economic and non-economic harm and the award was only five times greater than the statutory civil fine that might have been imposed). *Compare* Schimizzi v. Illinois Farmers Ins. Co., 928 F. Supp. 760 (N.D. Ind. 1996) (finding that $600,000 award was excessive because the defendant's tortious conduct did not consist of reckless disregard for health and safety; further, disparity between actual and punitive damages was great—thirteen times actual damages, and award was disproportionate as compared to criminal and civil penalties imposed under Indiana law).

194. 118 S. Ct. 1708 (1998).

195. *See id.* at 1712.

196. *Id.* at 1717.

197. *See id.* at 1712-13.

198. *Id.* at 1718.

Massachusetts v. Massachusetts General Hospital[199] used a deliberate indifference standard in determining the constitutional adequacy of medical care provided to pre-trial detainees, in *Whitley v. Albers*,[200] it held that in the context of correction officers' actions during a prison riot a standard of *purposeful harm* is necessary.[201] The *Lewis* Court explained that since deliberate indifference implies the opportunity for actual deliberation, it should not be applied to prison guards or police officers who face a situation calling for fast action where competing factors must be weighed in haste and under pressure.[202] Thus, the Court determined that "high-speed chases with no intent to harm suspects physically or to worsen their legal plight do not give rise to liability under the Fourteenth Amendment . . . ."[203] Because the plaintiff in *Lewis* did not allege that the deputy acted with "intent to harm," the lawsuit failed to meet the shocks the conscience test and thus had to be dismissed.[204]

Lewis establishes that a "shocks the conscience" standard must be met to make out a substantive due process case alleging abuse of executive power.[205] More specifically, it clarifies that a police officer does not violate substantive due process by causing death through deliberate or reckless indifference to life in a high-speed auto chase aimed at apprehending a suspected offender because under such circumstances actual deliberation is impossible and thus "a purpose to cause harm" must be proven.[206] On the other hand, where there is time for deliberation a deliberate indifference standard may be appropriate. Applying the lessons of *Lewis*, the Seventh Circuit in *Armstrong v. Squadrito*[207] ruled that a sheriff's conduct in holding a detainee for 57 days pursuant to a civil body attachment warrant, without an appearance before a magistrate, shocks the judicial conscience and is, therefore, actionable under the substantive due process clause.[208] The court explained that in the prison context forethought about an inmate's welfare is feasible and in fact is constitutionally required, and thus deliberate indifference is the appropriate standard.[209] The court first determined

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199. 463 U.S. 239 (1983).

200. 475 U.S. 312 (1986).

201. *Id.* at 320-21.

202. *Lewis*, 118 S. Ct. at 1719-20.

203. *Id.* at 1720.

204. *See id.* at 1721. In *Mays v. City of East St. Louis*, 123 F.3d 999 (7th Cir. 1997), the court flatly rejected *any* substantive due process challenge to a police officer's high-speed pursuit of a vehicle resulting in injury: "This nation's social and legal traditions do not give [automobile] passengers a legal right . . . to have police officers protect them by letting criminals escape." *Id.* at 1003. This same approach is reflected in the concurring opinion of Justices Scalia and Thomas in *Lewis*. They argued that the plaintiff's claim lacked any historical or textual support as a constitutional cause of action. *Lewis*, 118 S. Ct. at 1724 (Scalia, J., concurring in judgment only).

205. *Lewis*, 118 S. Ct. at 1716.

206. *Id.* at 1720.

207. 152 F.3d 564 (7th Cir. 1998).

208. *Id.* at 582.

209. *Id.* at 576-77.

that prolonged detention, even pursuant to a valid arrest, implicates a protected interest under substantive due process.[210] Although Indiana's body attachment statute does not itself create a substantive due process right, the procedures set forth in the law are relevant in assessing whether lack of prompt appearance offends federal due process.[211] Because under Indiana law a sheriff has exceedingly limited authority pursuant to a writ of attachment and is required to bring an arrestee immediately before the Circuit Court, the prolonged detention "represents an affront to substantive due process."[212] The court determined that Allen County's failure to ensure that arrestees be promptly brought before a magistrate demonstrated deliberate indifference to the rights of those arrested with a civil warrant.[213] At minimum, the plaintiff presented facts establishing that the jail had a policy or custom of refusing to accept complaint forms from detainees requesting information on their status.[214] In short, the court concluded that what happened to Walter Armstrong "shocks the conscience."[215]

Other questions remain unanswered regarding when tortious conduct rises to the level of a *constitutional tort*.[216] Of particular difficulty are cases involving misconduct by private parties where the injured plaintiff accuses the government of failing to act to prevent harm. For example, in *Stevens v. Umsted*,[217] the court rejected claims brought by a child who was repeatedly sexually assaulted by another student at the Illinois School for the Visually Impaired, even after the superintendent was put on notice of the assault. The court reasoned that the state did not take the child into custody, did not confine him against his will, and did not create the danger or render him more vulnerable to an existing danger.[218] Following Supreme Court precedent, the Seventh Circuit ruled that "'[i]naction

210. *Id.* at 573.

211. *See id.* at 575.

212. *Id.* at 576.

213. *Id.* at 579.

214. *Id. Compare* Tesch v. County of Green Lake, 157 F.3d 465, 475-76 (7th Cir. 1998) (finding that although deliberate indifference is the appropriate standard for substantive due process claims alleging failure to attend to handicapped pre-trial detainee's physical and medical needs, district court properly granted summary judgment under the facts of the case; the plaintiff presented no evidence suggesting that jail officials knew placing him in a cell that provided limited access to toilet and sink and no access to a shower for a 44-hour period would cause him any harm).

215. *Armstrong*, 152 F.3d at 582.

216. One question that has been fairly well resolved in this circuit is that deprivations of property, rather than liberty, ordinarily will not be actionable at all on a substantive due process theory, at least where state remedies are available. Thus, in *Centres, Inc. v. Town of Brookfield*, 148 F.3d 699, 704 (7th Cir. 1998), the court rejected plaintiff's claim that the government acted in an arbitrary and capricious fashion in denying him a building permit. Because federal courts should not be viewed as "zoning boards of appeal," a plaintiff must allege that some other substantive constitutional right has been violated or that state remedies are inadequate to survive dismissal for failure to state a claim. *See id.*

217. 131 F.3d 697, 701-06 (7th Cir. 1997).

218. *Id.* at 704-06.

by the state in the face of a known danger is not enough to trigger the obligation [to protect private citizens from each other]."'[219] The superintendent simply had no constitutional duty to protect the child. In contrast, the Supreme Court has ruled that where the state actually takes someone into custody, e.g., placing persons in its prisons or its mental institutions, there is a constitutional duty to guarantee conditions of reasonable care and safety.[220] Relying on this case precedent, the Indiana Supreme Court in *Ratliff v. Cohn*,[221] rejected the state's motion to dismiss a fourteen-year-old inmate's substantive due process claim that she had been subjected to hostility and threats by adult inmates and that she feared for her safety.[222]

C. *Equal Protection*

The Supreme Court in *Miller v. Albright*,[223] upheld the constitutionality of a federal statute that grants foreign-born children automatic citizenship status where the mother is a U.S. citizen, but that mandates proof of paternity by age eighteen where the father is a U.S. citizen. Miller was born out of wedlock in the Philippines to a Filipino national and an American citizen who was serving in the U.S. military at the time the child was conceived. The father never married the petitioner's mother and never returned to visit the child.[224] Although the father did later secure a paternity decree, he failed to do so before the child reached age eighteen as required by the federal statute. The father and petitioner then challenged the statute's different treatment of citizen fathers. After dismissing the father for lack of standing, both lower courts held against the petitioner.[225]

Six Justices rejected the equal protection challenge to the statute, but there was no majority opinion. Although this was the first gender-based statute to withstand constitutional challenge since the 1980s, only two Justices held that the law survived the fairly stringent standard mandating that government prove its classification scheme bears a fair and substantial relation to an important government interest.[226] Justice Stevens and Chief Justice Rehnquist reasoned that "biological differences between single men and single women provide a relevant basis for differing rules governing their ability to confer citizenship on children born out of wedlock in foreign lands."[227] They contended that the statute was not a tainted product of "overbroad stereotypes."[228] Further, the

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219. *Id.* at 705 (quoting Reed v. Gardner, 986 F.2d 1122, 1125 (7th Cir. 1993) (alteration in original)).
220. Youngberg v. Romeo, 457 U.S. 307, 324 (1982).
221. 693 N.E.2d 530 (Ind. 1998).
222. *Id.* at 547.
223. 118 S. Ct. 1428 (1998).
224. *See id.* at 1433.
225. *See id.* at 1433-34.
226. *Id.* at 1440.
227. *Id.* at 1442.
228. *Id.* at 1437.

different treatment met the intermediate scrutiny applied in gender-bias suits because the government had an important interest in ensuring reliable proof of a biological relationship between a potential citizen and the citizen-parent.[229] Congress also had an important interest in encouraging the development of a healthy relationship between the two while the child is a minor.[230]

Justices Scalia and Thomas concurred for a wholly unrelated reason. They reasoned that the remedy sought, namely conferral of citizenship on a basis other than that proscribed by Congress, went beyond the powers of federal courts.[231] Taking yet another approach, Justices O'Connor and Kennedy concurred on grounds that the petitioner did not have standing to raise her father's gender discrimination claim and her own claims were subject only to rational basis analysis.[232] While rejecting Justice Stevens' conclusion that the provision withstands heightened scrutiny, Justice O'Connor concluded that the gender discrimination claim was not properly before the Court.[233]

Three Justices in dissent argued that this disparate treatment of fathers and mothers reinforced stereotypical, historic patterns and could not survive heightened scrutiny. Justice Ginsburg cited well established case precedent that a gender-neutral classification should be used where it can accomplish the government's goal.[234] Here the government can ensure that only children who have established at least minimal contact with the citizen-parent during their early and formative years will qualify for citizenship, without using a gender-based classification.[235] Justice Breyer opined that the statutory distinctions were based on a generalization that "mothers are significantly more likely than fathers to care for their children, or to develop caring relationships with their children."[236] Any concerns about false paternity claims were easily resolved by mandating inexpensive DNA testing that could prove paternity with certainty.[237]

Although the decision seems to fly in the face of recent Supreme Court cases mandating "an exceedingly persuasive" justification for gender-based distinctions,[238] it is uncertain how the Court would have ruled had the father remained a party to the action. Arguably, Justices O'Connor and Kennedy may have joined the three dissenters to reach the opposite conclusion. Indeed it is important to note that only two Justices justified the disparity based on the biological differences between the sexes. In fact, both Justices Breyer and Ginsburg cite to Justice O'Connor's concurring view that gender classifications based on stereotypes cannot survive heightened scrutiny. They conclude that a

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229. *See id.* at 1438.
230. *See id.* at 1439.
231. *Id.* at 1446-48 (Scalia, J., concurring).
232. *Id.* at 1442-46 (O'Connor, J., concurring).
233. *Id.* at 1445.
234. *Id.* at 1454 (Ginsburg, J., dissenting).
235. *See id.*
236. *Id.* at 1461 (Breyer, J., dissenting).
237. *See id.* at 1462.
238. *See* United States v. Virginia, 518 U.S. 515, 531 (1996).

majority of the Court really does not share Justice Stevens' assessment of the law on the merits.[239]

D. Free Speech and Association Rights

1. Commercial Speech.—Since 1976, the Supreme Court has recognized that commercial speech falls within the umbrella of the First Amendment although it has never afforded commercial speech the full protection of non-commercial speech. Because commercial speech is protected only to the extent it conveys truthful information to consumers, the state may ban such speech if it is false, deceptive, or misleading, or if it concerns unlawful activity. Further, in *Central Hudson Gas & Electric v. Public Service Commission*,[240] the Court held that even truthful, non-misleading commercial speech may be subject to state regulation, provided the law directly and materially advances a substantial governmental interest in a manner no more extensive than necessary to serve that interest.[241]

In *Wallace v. Brown County Area Plan Commission*,[242] the court applied this four-prong analysis to sustain a town ordinance banning neon signs. The Wallaces, who installed a neon "OPEN" sign in the front of their restaurant, conceded that the ordinance sought to implement a substantial government interest, namely the interest of the town in aesthetics and safety.[243] As in most commercial speech cases, the dispute arose over "whether the ordinance directly advance[d] the interests of safety and aesthetics, and whether the ordinance reach[ed] further than necessary to accomplish those objectives."[244] The Wallaces complained "that the [t]own submitted no evidence to show that the neon sign create[d] a distraction to pedestrians and motorists or that the [t]own's aesthetic image [was] harmed by their sign."[245] At minimum, they contended a genuine issue of material fact existed on these points and thus the trial court erred in granting summary judgment in the town's favor.[246]

Rejecting these arguments, the court pointed to the law's preamble in which the plan commission asserted its concerns regarding public safety and welfare.[247] The sign ordinance had been enforced for over twenty-five years and during that time the town board had "consistently cited the unique scenic and architectural characteristics of the town and concerns for public safety as the reason for enacting the ordinance."[248] Finally, the court concluded that the law was not

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239. *Miller*, 118 S. Ct. at 1457-58 (Breyer, J., dissenting); *id.* at 1450 (Ginsburg, J., dissenting).

240. 447 U.S. 557 (1980).

241. *Id.* at 566.

242. 689 N.E.2d 491 (Ind. Ct. App. 1998).

243. *See id.* at 493.

244. *Id.*

245. *Id.*

246. *See id.*

247. *Id.* at 494.

248. *Id.*

more extensive than necessary, citing Supreme Court precedent that the "fit" between the restriction and the government interest need only be reasonable.[249] The town contended that because Nashville covers a geographically small area, it could not limit neon signs to any particular area. Further, no certain type of neon sign would be less distracting, whereas alternatives were open to the Wallaces, such as ground-lighted signs that would not adversely affect the aesthetic concerns of the community.[250]

A somewhat more complicated commercial speech issue was addressed in *Ad Craft, Inc. v. Board of Zoning Appeals*.[251] The Area Plan Commission of Evansville and Vanderburgh County (the "APC") had a sign ordinance, which required that a permit be obtained before a sign could be "erected" or "placed."[252] The plaintiffs in this case were simply altering the sign of their customer, a realty company, which, having merged with another company, directed Ad Craft to change the sign to reflect the new entity.[253] The court first rejected Ad Craft's argument that the sign ordinance did not even apply to alteration of an existing sign. Adopting the position of the Board of Zoning Appeals ("BZA"), the court held that the statute applied because when an existing sign is "altered" a different sign is "placed" or "erected" in its stead and thus a permit must first be secured.[254]

Addressing the constitutional issue, the court applied the *Central Hudson*[255] test and concluded that the permit application requirement directly advanced the governmental interests in aesthetics and traffic safety by "providing notice to the APC of sign changes that its investigators may otherwise miss."[256] The court further concluded that the ordinance reached no further than necessary to accomplish that interest. As to the latter, Ad Craft argued that the BZA was attempting to regulate the content of its speech, which, even as to less protected commercial speech, is generally impermissible.[257] The Supreme Court in *Central Hudson* cautioned that a government entity can regulate only certain non-communicative aspects of commercial expression for purposes such as aesthetics and traffic safety.[258] Further, in *44 Liquormart v. Rhode Island*,[259] the Court held that where government seeks to suppress truthful, non-misleading information for paternalistic reasons, e.g., it wants to stop the public from purchasing the item,

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249. *Id.* (citing Board of Trustees v. Fox, 492 U.S. 469, 480 (1989)).
250. *See id.*
251. 693 N.E.2d 110 (Ind. Ct. App. 1998).
252. *Id.* at 114.
253. *See id.* at 112.
254. *Id.* at 115.
255. Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n of N.Y., 447 U.S. 557 (1980).
256. *Ad Craft*, 693 N.E.2d at 117.
257. *See id.* at 116-17.
258. *Central Hudson*, 447 U.S. at 563 n.5.
259. 517 U.S. 484 (1996).

the *Central Hudson* test must be applied with "special care."[260] In that case, the Supreme Court invalidated a statute that banned advertisement of retail liquor prices except at the place of sale.[261] In *Ad Craft*, the court found the BZA was not attempting to regulate the content of Ad Craft's speech. Even though it was a change in the message that triggered the ordinance, it was not the content of the message that concerned the APC. The APC wanted to ensure that the alteration of the sign did not affect the physical characteristics of the sign that had been allowed under a previously-obtained permit.[262] Because the purpose of the permit requirement was unrelated to content and was administered without reference to content, the court viewed this as a valid regulation of commercial speech.[263]

2. *Free Speech and Association Rights of Government Employees.*—The United States Supreme Court has held that the government cannot condition employment upon relinquishing First Amendment rights.[264] However, it has also recognized that speech rights of government employees are not the same as those of the public at large. Rather, courts must balance "the interests of the [employee], as a citizen, in commenting upon matters of public concern and the interests of the State, as an employer, in promoting the efficiency of the public services it performs . . . ."[265] In *Connick v. Myers*,[266] the Court refined the balancing test, clarifying that judges must make an initial inquiry as to whether the government employee's speech is a matter of public concern, because "private" speech is entitled to little, if any, First Amendment protection. The Court directed judges to examine the form, content, and context of the speech, describing speech upon matters of public concern as "relating to any matter of political, social, or other concern to the community."[267] As to the balancing test, the Supreme Court explained in *Waters v. Churchill*,[268] that "[w]hen someone who is paid a salary so that she will contribute to an agency's effective operation begins to do or say things that detract from the agency's effective operation, the government employer must have some power to restrain her."[269]

In several cases, state and federal courts took a fairly liberal approach in finding that the speech in question was at least partially of public concern; however, they upheld imposing sanctions for the speech under the *Connick* balance. For example, in *Messman v. Helmke*,[270] the court held that a collective

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260. *Id.* at 485-86, 504.

261. *Id.* at 499-500.

262. *Ad Craft*, 693 N.E.2d at 117.

263. *Id.*

264. *See* Keyishian v. Board of Regents, 385 U.S. 589, 605-06 (1967).

265. United States v. National Treasury Employees Union, 513 U.S. 454, 465-66 (1995) (citing Pickering v. Board of Educ., 391 U.S. 563, 568 (1968)).

266. 461 U.S. 138 (1983).

267. *Id.* at 146.

268. 511 U.S. 661 (1994).

269. *Id.* at 675.

270. 133 F.3d 1042 (7th Cir. 1998).

bargaining provision prohibiting city firefighters from participating in non-city firefighting organizations addressed a matter of public concern. The court acknowledged that associating with firefighting organizations in Ft. Wayne's surrounding communities had taken on "a political sheen," because associating with the volunteer fire departments supported the political goal of opposing annexation by Ft. Wayne of the surrounding communities.[271] Applying the *Connick* balance, however, the court determined that the firefighters' interest in participating in non-city firefighting organizations was outweighed by the city's interests in reducing off-duty injuries, avoiding conflicts in firefighters' duties, and minimizing liability for paid sick leave.[272] The court determined that interference with work, personnel relationships, or job performance detracts from the public employer's function and that avoiding such interference can be a strong state interest.[273] Relying on *United States v. National Treasury Employees Union*,[274] the firefighters argued that the interests propounded by the city were unsupported by any evidence and that the prohibition impermissibly singled out their off-duty firefighting activities when the same harm to the city's interests could result from many other off-duty occupations that were not prohibited.[275]

The court distinguished *National Treasury*, which involved a flat ban on 1.7 million federal employees from accepting honoraria from anyone for speaking on any topic regardless of how remote from their jobs. In that case, the Supreme Court concluded that the nexus between the government interest and the speech at issue was simply too tenuous to support the all-out ban on speech.[276] In contrast, the ban on off-duty firefighting was closely related to the harms Ft. Wayne wished to avoid. Further, this was not a blanket restriction on speech and the firefighters were still free to voice their support for the unannexed communities.[277] In short, the court concluded that the city's interest in efficiency

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271. *Id.* at 1045.

272. *Id.* at 1045-47. The court applied the balancing test, though noting that a question has been raised as to whether *Connick* is useful in cases involving freedom of association rather than free speech. *Id.* at 1046 n.3. On the same day this case was decided, the court ruled in *Balton v. City of Milwaukee*, 133 F.3d 1036, 1039-40 (7th Cir. 1998), that despite the split in the circuits, it will apply the *Connick* balancing test to a freedom of association claim. The *Balton* court concluded that retaliatory action taken against employees for failing to pay dues to an officers' association did not violate First Amendment rights where their disillusionment with the Chiefs Association had nothing to do with its political, social, or religious goals, but was based purely on issues of individual economic importance. *Id.* at 1040.

273. *Messman*, 133 F.3d at 1047.

274. 513 U.S. 454 (1995).

275. *See Messman*, 133 F.3d at 1047.

276. *See id.* (citing United States v. National Treasury Employees Union, 513 U.S. 454 (1995)).

277. *See id.* at 1047-48. The union's constitution prohibited advocacy, or membership in, other firefighting organizations, but the court concluded that the conduct of the union was not state action and there was no evidence supporting any type of joint action between Ft. Wayne's contract with its firefighters and the union's adoption of its constitution, which was enacted at least four

and fiscal responsibility outweighed the firefighters' associational rights.

Similarly, in *Davidson v. City of Elkhart*,[278] the court ruled that even though a police officer's statements to the press regarding the department's ongoing investigation of a controversial shooting was of public concern, his termination for releasing the information without authorization did not violate the First Amendment.[279] The court determined, as a matter of law, that the disruptiveness of the officer's conduct, which "threatened to undermine the authority and credibility of both the Elkhart Police Department and the County Prosecutor's Office," by making it appear that the outcome of the investigation was predetermined, outweighed any value his speech might have had.[280]

Where political affiliation alone, unaccompanied by other forms of expression, is the basis for the adverse employment action, the Supreme Court has applied a different analysis. In *Elrod v. Burns*[281] and *Branti v. Finkel*,[282] the Court held that government officials may not discharge public employees for refusing to support a political party or its candidates unless political affiliation is a reasonably appropriate requirement for the job in question.[283] Once an employer has established that protected association was a motivating factor in the government's decision, the burden shifts to the government to prove that political affiliation is "an appropriate requirement for the effective performance" of the job in question.[284]

In *Nelms v. Modisett*,[285] a field investigator in the Consumer Protection Division ("CPD") of the office of the Indiana Attorney General claimed he was terminated because of his political affiliation some six months after a Democrat was elected Attorney General. The court held that Nelms did not even establish a *prima facie* case of politically-motivated discharge.[286] Nelms' superiors argued that they were reorganizing the CPD and found it necessary to reduce the role of field investigators, and the individual who was retained had more seniority and more exemplary work habits than Nelms.[287] Although Nelms cited a comment by one of his superiors that "you understand political realities," the court deemed this insufficient and generally stated that an employee cannot rely on speculation

years before the collective bargaining agreement provision came into being. *Id.* at 1044-45.

278. 696 N.E.2d 58 (Ind. Ct. App. 1998).

279. *Id.* at 62.

280. *Id. Compare* Lickiss v. Drexler, 141 F.3d 1220, 1222-23 (7th Cir. 1998) (finding that deputy sheriff who raised questions about the defendants' official investigation of the activity of another officer was addressing a matter of public concern; *Connick* balance weighed in favor of the employee, especially where plaintiff was not a confidential employee or policy-maker and had a duty to report the information to his superiors).

281. 427 U.S. 347 (1976).

282. 445 U.S. 507 (1980).

283. *Branti*, 445 U.S. at 518; *Elrod*, 427 U.S. at 349.

284. *Branti*, 445 U.S. at 518.

285. 153 F.3d 815 (7th Cir. 1998).

286. *Id.* at 819.

287. *See id.*

or opinions of non-decision-makers as proof that a firing was impermissibly motivated by political affiliation.[288] In short, the defendants proffered a legitimate, nonpolitical reason for the termination, and the plaintiff did not present evidence casting doubt on that reason.

In a second case, *Kline v. Hughes*,[289] the court rejected the political patronage claim brought by a former deputy auditor. Looking to Indiana law, the court determined that the deputy county auditor performs all the official duties of the county auditor and thus plays a vital role in the implementation of the county auditor's policies.[290] Although Kline argued that she should be protected because the duties she actually performed as deputy auditor did not involve any policy-making discretion, Seventh Circuit case precedent makes it clear that the powers inherent in the office, rather than the duties performed by a particular officeholder, are controlling.[291] Thus, as a matter of law, her position was not protected by the First Amendment.

3. Free Speech Rights of the Media.—The U.S. Supreme Court, as well as lower federal and state courts, addressed questions related to freedom of the press. Although the First Amendment to the U.S. Constitution specifically guarantees freedom of the press, the Supreme Court has been reluctant to recognize any type of press privilege. Thus, in *Branzburg v. Hayes*,[292] the Court held that reporters called to testify before a grand jury do not enjoy a First Amendment privilege to refuse disclosure of confidential sources or information gathered in the course of reporting.[293] The Court reasoned that subjecting reporters, like private citizens, to subpoenas did not intrude upon speech, did not restrict what the press may publish, and did not mandate the press to publish anything that it preferred to withhold.[294] Despite the Supreme Court's pronouncement, several lower federal and state court decisions have recognized a "qualified" reporter's privilege based on Justice Powell's concurring opinion, which provided the crucial fifth vote rejecting the privilege.[295] Justice Powell urged a "proper balance" be struck between the interests of the press and the duty of all citizens to give evidence in criminal proceedings.[296] Some courts have interpreted this dictum to mandate some extraordinary showing of relevance and necessity before disclosure is compelled.[297]

In a case of first impression, the Indiana Supreme Court in *In re WTHR-TV*

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288. *Id.*

289. 131 F.3d 708 (7th Cir. 1997).

290. *Id.* at 710.

291. *See id.*

292. 408 U.S. 665 (1972).

293. *Id.* at 697.

294. *Id.* at 700-01.

295. *Id.* at 709 (Powell, J., concurring).

296. *Id.* at 709-10 (Powell, J., concurring).

297. *See* RODNEY A. SMOLLA, SMOLLA AND NIMMER ON FREEDOM OF SPEECH 13.03[30] n.34 (1994) (listing cases accepting a reporter's privilege). *See also In re* WTHR-TV, 693 N.E.2d 1, 12 n.11 (Ind. 1998) (citing cases accepting a reporter's privilege).

v. Cline,[298] rejected this line of cases, opining that those decisions construing *Branzburg* to recognize a qualified reporter's privilege misread the Supreme Court decision. In *Branzburg*, Justice Powell cautioned lower courts not to read *Branzburg* as eviscerating all First Amendment protection for newsgathering, yet he specifically rejected the qualified press privilege urged by four dissenting Justices.[299] The Indiana Supreme Court reasoned that nothing in Supreme Court precedent, nor any policy arguments, justified granting such a privilege.[300] It therefore rejected the station's claim that it could not be forced to disclose unaired video footage, which recorded an interview with a juvenile charged with murder. Relying upon the test adopted by those courts that had granted a qualified privilege, the station argued that the plaintiff should have to show the information was "clearly material and relevant" to her defense, that it was "critical to the fair determination" of her case, and that she had "exhausted all other sources for the same information."[301] Because this was precisely the protective standard rejected by the majority in *Branzburg*, the Indiana Supreme Court denied the station's position.[302]

More broadly, the court reasoned that First Amendment values do not compel recognition of a privilege. Since *Branzburg*, the press does not appear to have been chilled, notwithstanding the obligation of reporters to give evidence in criminal proceedings.[303] The court also rejected the notion that compelled disclosure of unaired footage might encourage prompt destruction of that data or that it would distract reporters and editors from doing their jobs. Although the court conceded that it might be possible to envision a situation in which compliance might be so time-consuming so as to undermine the ability to report the news, here the plaintiff sought only a copy of the full interview conducted with her while she was in police custody, and there was no reason to suppose that compliance would impose any significant burden.[304] In addition, because claims of abuse of the discovery process can be made on a case-by-case basis, the mere possibility of abuse does not justify blanket immunity from discovery: "Unless and until this horrible shows up at a real parade, we are unwilling to assume it as a basis for decision."[305] Thus, when information regarding a criminal case is demanded from a reporter, the First Amendment simply does not require in every case that a special showing of need and relevance be made beyond that imposed under normal discovery rules.

Alleged interference with the press' ability to gather the news was likewise

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298. 693 N.E.2d 1 (Ind. 1998). *See also supra* notes 58-65 (rejecting the state constitutional basis for the discovery request).

299. *Branzburg*, 408 U.S. at 709-10 (Powell, J., concurring).

300. *In re WTHR-TV*, 693 N.E.2d at 12.

301. *Id.* at 10.

302. *Id.*

303. *See id.* at 13.

304. *Id.* at 13-14.

305. *Id.* at 14.

rejected in *South Bend Tribune v. Elkhart Circuit Court*.[306] In another matter of first impression, the Indiana Court of Appeals held that a gag order placed on participants in a local murder trial did not constitute an impermissible restraint on the media's ability to gather the news.[307] Although the United States Supreme Court has held that a gag order on the press is barred by the First Amendment absent a showing of a clear and present danger of prejudicial impact,[308] in *South Bend Tribune* the gag order was placed solely upon trial participants, and thus the defendant judge did not have to meet the stringent standard.[309] Further, the appellate court maintained that the order was justified because pre-trial publicity likely threatened the defendant's Sixth Amendment right to a fair trial.[310]

The press fared much better in a case brought before the United States Supreme Court, but the issues were significantly different because the broadcaster was a publicly owned television station. Despite allegations of government censorship of speech,[311] the Court in *Arkansas Education Television Commission v. Forbes*, held that the public television station had discretion to exclude from a televised congressional election debate a candidate who generated insufficient public interest.[312]

Because the station was publicly owned, the Supreme Court first addressed the question of "forum."[313] Regulation of speech on government owned property, such as streets and parks, is subjected to a strict test, which requires that the regulation be content-neutral and narrowly tailored to achieve a significant public interest while leaving open ample alternative means for the message to be communicated.[314] For example, in *Ayres v. City of Chicago*,[315] the court affirmed a preliminary injunction against enforcement of a peddler's ordinance, which prevented an organization from selling t-shirts at a city-sponsored park festival. The court ruled that even if the regulation served important government interests in controlling congestion, as well as aesthetics, the no peddling zone was much too broad and the government's interests could have been served by simply fixing certain locations near the park or limiting the size of the plaintiff's peddling operation.[316]

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306. 691 N.E.2d 200 (Ind. Ct. App. 1998).

307. *Id.* at 201.

308. *See* Nebraska Press Ass'n v. Stuart, 427 U.S. 539 (1976).

309. *See South Bend Tribune*, 691 N.E.2d at 201-02. The defendant relied on *Application of Dow Jones & Co. v. Simon*, 842 F.2d 603 (2nd Cir.), *cert. denied*, 488 U.S. 946 (1988), for its determination that its gag order did not constitute a prior restraint. The Second Circuit drew the same distinction between gag orders imposed on the press and gag orders imposed on trial participants. *Id.* at 609.

310. *South Bend Tribune*, 691 N.E.2d at 203.

311. Arkansas Educ. Television Comm'n v. Forbes, 118 S. Ct. 1633 (1998).

312. *Id.* at 1640.

313. *Id.* at 1640-41.

314. *See* Ward v. Rock Against Racism, 491 U.S. 781, 791 (1989).

315. 125 F.3d 1010 (7th Cir. 1997).

316. *Id.* at 1016.

On the other hand, in *Potts v. City of Lafayette, Indiana*,[317] the court sustained an order imposing a "weapons" ban on attendees of a Ku Klux Klan ("KKK") rally that included tape recorders carried by attendees without a media pass and any other objects that might be thrown.[318] The court first ruled that the regulation was not aimed at the content of the views aired at the rally.[319] In addition, the goal of preventing violence and injury would have been achieved less effectively absent regulation, although other items such as belt buckles and shoelaces were permitted.[320] Further, the order left open ample alternative channels of communication.[321] The court emphasized that KKK rallies by their very nature breed violence and in fact, such violence had erupted at earlier KKK demonstrations.[322] The court emphasized that significant discretion must be given police officers who have to make "instantaneous judgment calls" in order to protect the public.[323]

In *Arkansas Education Television Commission v. Forbes*,[324] the Supreme Court decided that even though the station was government owned, and even though candidate debates are "of exceptional significance in the electoral process," the station was not regulating speech in a traditionally public forum like a park or street.[325] Further, since the station never generally "opened" the debate, it could not be considered a "designated" public forum.[326] The Court therefore concluded that this was a non-public forum, which is held to a less restrictive First Amendment analysis.[327] The government can exclude speakers from non-public forums provided its reasons are viewpoint-neutral and the regulation is reasonable in light of the property's purpose.[328] Here the Court found ample evidence to support the jury's finding that Mr. Forbes was not excluded because of his political views, but because he lacked a campaign organization and popular support.[329] Further, the station's regulation was reasonable in that limiting debate to major party candidates and other candidates with strong popular support ensures that the views of serious contenders will be

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317. 121 F.3d 1106 (7th Cir. 1997).

318. *Id.* at 1114.

319. *Id.* at 1111.

320. *See id.* at 1111-12.

321. *See id.* at 1112. The court relied on the special information-gathering function of the press to sustain this form of discrimination; the attendees were not permitted to bring in tape recorders, pens, etc., whereas the press was so permitted, to reasonably accommodate the First Amendment rights of the press. *See id.*

322. *Id.*

323. *Id.*

324. 118 St. Ct. 1633 (1998).

325. *Id.* at 1640-41.

326. *See id.* at 1642.

327. *Id.* at 1641-42.

328. *See id.* at 1643.

329. *Id.* at 1643-44.

heard.[330] The Court noted that if all speakers are allowed access, stations might choose not to air them at all in order to avoid a choice between "cacophony, on the one hand, and First Amendment liability, on the other."[331] In short, the decision to exclude Forbes, an independent candidate with little popular support, was a reasonable, viewpoint-neutral exercise of journalistic discretion consistent with the First Amendment.[332]

4. Government Funding of Speech.—The Supreme Court has held that the government has more leeway under the First Amendment in choosing to fund certain speech than it does in directly regulating or penalizing speech. On the other hand, the government may not attempt to suppress particular viewpoints in making funding decisions, and it cannot justify viewpoint discrimination among private speakers based on economic scarcity. Thus, in *Rosenberger v. Rector & Visitors of University of Virginia*,[333] the Court held that a state university violated the First Amendment in denying student activity funds to a religious journal where the subsidy was widely available to all student organizations that met the objective criterion that the activity be related to the university's educational purpose.[334]

In *National Endowment for the Arts v. Finley*,[335] the Supreme Court distinguished *Rosenberger* and sustained selective funding of the arts. In the wake of public outrage at the National Endowment for the Arts' (the "NEA") award of grants, which funded homoerotic photographs by Robert Mapplethorpe and a photograph of a crucifix immersed in artist's Adres Serrano's urine, the federal law was amended in 1990 to add a clause admonishing the NEA to take "decency and respect" into consideration in determining whether the grant statute's criteria of "artistic excellence" and "artistic merit" are met.[336] Citing to the legislative history, the Supreme Court noted that this statutory amendment was actually a "bipartisan proposal introduced as a counterweight to amendments aimed at eliminating the NEA's funding or substantially constraining its grant-making authority."[337] Viewed in this light, the Court determined in an 8-1 decision that the amendments were constitutional.[338]

The Court contrasted *Rosenberger*, where funds were widely available to all student organizations, with the NEA funding, which is a highly competitive

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330. *See id.* at 1644.

331. *Id.* at 1643.

332. The Court noted that most public broadcasting should not be subjected to any scrutiny under the First Amendment because this would be antithetical to editorial discretion that broadcasters must exercise. Because, however, candidate debates are by design a forum for political speech, and they are of exceptional significance in the electoral process, the Court proceeded to apply First Amendment forum analysis. *Id.* at 1640.

333. 515 U.S. 819 (1995).

334. *Id.* at 845-46.

335. 118 S. Ct. 2168 (1998).

336. *See id.* at 2172-73.

337. *Id.* at 2176.

338. *Id.* at 2180.

process whereby the NEA must make aesthetic judgments as well as the inherently content-based "excellence" threshold to support any grant.[339] Although conceding that the terms of the statute are "undeniably opaque," the Court found the law unlikely to compel speakers "to steer too far clear of any 'forbidden area' in the context of grants of this nature."[340] Further, it emphasized that even some chilling effect on speech is less objectionable where the government acts as patron rather than sovereign.[341] Although the majority took pains to conclude that the "decency and respect" criteria did not prohibit any particular viewpoint, Justices Scalia and Thomas in a concurring judgment contended that the law clearly discriminated on the basis of content and viewpoint but that it was nonetheless "perfectly constitutional" because taxpayers should not be forced to subsidize art that conveys an offensive message.[342]

E. Freedom of Religion

The First Amendment guarantees both that Congress makes no law respecting an establishment of religion and that it not interfere with the free exercise of religion.[343] Together the clauses have been interpreted as mandating that government maintain a position of neutrality vis-a-vis religion. Defining what constitutes "a neutral position" has proved troublesome. As to the Establishment Clause, the Supreme Court in the early 1970's, in *Lemon v. Kurtzman*,[344] held that government programs must have a secular purpose, their primary effect may neither advance nor inhibit religion, and any government program may not create excessive entanglement between church and state.[345] In recent years several Justices have vociferously argued that the *Lemon* test is too restrictive and that it should be replaced by a more "accommodationist" approach to church-state questions.[346] Justice O'Connor has argued that the Establishment Clause is violated only where the government has endorsed or demonstrated approval of religion,[347] while Justice Scalia would find a violation only when government discriminates among religious organizations or imposes coercive pressure to engage in religious activities.[348]

In *Agostini v. Felton*,[349] the Supreme Court, while not formally overturning *Lemon*, rejected earlier Supreme Court opinions that applied *Lemon*, announcing

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339. *Id.* at 2178.

340. *Id.* at 2179.

341. *Id.*

342. *Id.* at 2180-85 (Scalia, J., concurring in judgment).

343. U.S. CONST. amend. I.

344. 403 U.S. 602 (1971).

345. *Id.* at 612-13.

346. *See* Lamb's Chapel v. Center Moriches Union Free Sch. Dist., 508 U.S. 384, 399-400 (1993) (Scalia, J., concurring).

347. Wallace v. Jaffree, 472 U.S. 38, 75 (1985) (O'Connor, J., concurring).

348. Lee v. Weisman, 505 U.S. 577, 637-44 (1992) (Scalia, J., dissenting).

349. 117 S. Ct. 1997 (1997).

that the older decisions could not be squared with the Court's intervening Establishment Clause jurisprudence.[350] The Supreme Court held that the federal government, pursuant to Title I of the 1965 Elementary and Secondary Education Act,[351] could fund remedial instruction and counseling for disadvantaged students in parochial schools without violating the Establishment Clause.[352] By a 5-4 vote, it held that sending publicly-paid teachers into religious schools to help students with such subjects as math, science, and English does not violate the constitutionally required separation between church and state.[353]

Similarly, in *Zobrest v. Catalina Foothills School District*,[354] the Court upheld providing a sign language translator for a deaf student attending Catholic school, even though the translator would make religious statements in some translations.[355] In both cases, the Court abandoned the presumption that public employees on parochial school grounds will inevitably inculcate religion or that their presence always constitutes a symbolic union between government and religion.

The Court in *Agostini* emphasized that providing Title I assistance would not create a financial incentive to undertake religious education. The aid was allocated on the basis of neutral, secular criteria, that neither favor nor disfavor religion, and the aid was available to all beneficiaries on a non-discriminatory basis.[356] The Court explained that aid to parochial schools will not be deemed to impermissibly advance religion if "it does not result in governmental indoctrination; define its recipients by reference to religion; or create an excessive entanglement."[357]

The immediate effect of *Agostini* was to allow public school districts to send public-salaried teachers into church-run schools to provide remedial educational services. Indiana litigants learned this year, however, that federal law does not *mandate* public schools to do so. In *K.R. by M.R. v. Anderson Community School Corp.*,[358] plaintiffs argued that the school district violated federal statutory law, namely the Individuals with Disabilities Education Act ("IDEA"),[359] as well as federal constitutional law, in refusing to provide disabled students attending private schools the same services it made available to those attending public schools.[360] Although the school board provided speech therapy, occupational

350. *Id.* at 2016-17.

351. 20 U.S.C. §§ 6301-8962 (1994 & Supp. III 1997).

352. *Agostini*, 117 S. Ct. at 2018-19.

353. *Id.* at 2013.

354. 509 U.S. 1 (1993).

355. *Id.* at 13-14.

356. *Agostini*, 117 S. Ct. at 2014.

357. *Id.* at 2016.

358. 125 F.3d 1017 (7th Cir. 1997), *cert. denied*, 118 S. Ct. 1360 (1998).

359. 20 U.S.C. §§ 1400-91o (1994 & Supp. III 1997).

360. The IDEA states only that services "may be provided . . . on the premises of private . . . schools." *Id.* § 1412 (1994). Thus, the court ruled that school districts have discretion in the matter. *K.R. by M.R.*, 125 F.3d at 1018. *Accord* Peter v. Wedl, 155 F.3d 992 (8th Cir. 1998);

therapy, and physical therapy at the public school site, which plaintiffs were permitted to attend, it did not offer services at the parochial school site. The court determined that this decision did not convey any message of government disapproval of religion nor did it infringe on K.R.'s right to fully exercise her religious choice.[361]

Agostini has also fueled the debate as to the constitutionality of school voucher programs whereby voucher checks are issued to students who can then select the elementary or secondary school of their choice, whether public or parochial. The Wisconsin Supreme Court in *Jackson v. Benson*,[362] upheld a state statute authorizing financial aid vouchers on the basis of religion-neutral eligibility criteria for low-income students in the Milwaukee area. Applying the *Lemon* analysis, the court determined the program had the secular effect of providing low-income children with the opportunity for a better education.[363] It survived the primary-effect prong based on the *Agostini* rationale that no impermissible effect should be found, provided the government has instituted a broad, neutral program that neither favors nor disfavors religion, and the aid occurs primarily as a result of private choices of parents and provides no financial incentive to choose a religious school.[364] Finally, the court determined that minimal oversight standards would not result in excessive church-state entanglement.[365]

A final development worth noting concerns the Religious Freedom Restoration Act ("RFRA").[366] Congress enacted this law in 1993 in direct response to the Supreme Court's decision in *Employment Division v. Smith*,[367] which held that a state may enforce laws of general applicability even where such laws infringe upon the free exercise of religion, provided such laws are rational.[368] Prior to *Smith*, laws that substantially burdened religious freedom were subject to a much stricter analysis—states had to show an overriding interest that would be significantly impaired by granting religious exemption. RFRA sought to restore this analysis by clarifying that government could not substantially burden a person's exercise of religion unless it demonstrates that the burden furthers a compelling interest and is the least restrictive means of furthering that interest.[369]

In *City of Boerne v. Flores*,[370] the Supreme Court struck down RFRA, ruling that Congress could not impose its own definition of constitutional liberties or

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Russman v. Board of Educ. of Watervliet, 150 F.3d 219 (2nd Cir. 1998).

361. *K.R. by M.R.*, 125 F.3d at 1019.
362. 578 N.W.2d 602 (Wis.), *cert. denied*, 119 S. Ct. 466 (1998).
363. *Id.* at 612.
364. *See id.* at 616-17.
365. *Id.* at 619.
366. 42 U.S.C. §§ 2000bb1-bb4 (1994).
367. 494 U.S. 872 (1990).
368. *Id.* at 879.
369. 42 U.S.C. § 2000bb(a).
370. 117 S. Ct. 2157 (1997).

make substantive changes in constitutional protections. Although Congress has the power under section 5 of the Fourteenth Amendment to pass laws that deter or remedy constitutional violations, the Court drew a distinction between the power to enforce, which is "remedial," and the power to determine what constitutes a constitutional violation.[371] The Court held that RFRA was so out of proportion to a supposed remedial or preventive objective that it could not be understood as responsive to any unconstitutional behavior.[372] Because it saddled states with a strict compelling interest/least restrictive means test, RFRA was a considerable congressional intrusion into the states' traditional authority to regulate for the health and safety of their citizens.[373]

Perhaps the most immediate impact of the Court's ruling was to alter the analysis in literally hundreds of cases, many of which were brought by prison inmates raising RFRA challenges to dress and grooming requirements and demanding accommodation of their religious-based dietary laws, among other things.[374] More recently several courts have questioned whether the Supreme Court invalidated RFRA only as applied to state government. In *Young v. Crystal Evangelical Free Church*,[375] the Eighth Circuit ruled that RFRA could constitutionally be applied to federal laws, including the law of bankruptcy.[376] Indeed, the court held that RFRA effectively amends section 548(a)(2)(A) of the Bankruptcy Code to bar a bankruptcy trustee from voiding debtors' tithes to their church as fraudulent transfers.[377] In accordance with their religious beliefs, the debtors had given a tenth of their income, or $13,450, to their church in the year before they filed a Chapter 7 bankruptcy petition. Although finding that such a transfer would be deemed a fraudulent transfer within the meaning of bankruptcy law, the court ruled that recovery of these contributions substantially burdened the debtors' free exercise of religion and, because it did not further a compelling government interest, it violated RFRA.[378] The court reasoned that *City of Boerne* did not affect its ruling, because there the Supreme Court addressed only the question of whether Congress exceeded its power under section 5 of the Fourteenth Amendment, but did not address whether Congress could, pursuant to its Article I authority, constitutionally impose RFRA on federal laws.[379]

After finding that the "portion of RFRA applicable to the federal government

371. *Id.* at 2164.

372. *Id.* at 2170.

373. *Id.* at 2169-71.

374. *See, e.g.*, Sasnett v. Sullivan, 91 F.3d 1018, 1023 (7th Cir. 1996) (once a prisoner has shown a substantial burden, the burden of justification is on the state; prison failed to justify flat ban on wearing jewelry as applied to religious crucifixes), *cert. granted*, 117 S. Ct. 2502 (1997), *vacated and remanded in light of* City of Boerne v. Flores, 117 S. Ct. 2157 (1997).

375. 141 F.3d 854 (8th Cir.), *cert. denied*, 119 S. Ct. 43 (1998).

376. *Id.* at 861.

377. *Id.*

378. *Id.* at 863.

379. *Id.* at 858.

is fully severable from the portion applicable to the states,"[380] the court ruled that RFRA was an appropriate means by Congress to modify the federal bankruptcy law.[381] The court also held that, as so construed, RFRA did not violate the Establishment Clause.[382] RFRA has the secular purpose of preserving everyone's free exercise rights, rather than benefitting a particular religious sect, accommodating religious practice does not impermissibly advance religion, and no excessive entanglement between church and state will result.[383]

The opinion seems misguided in light of *City of Boerne*'s apparent holding that Congress, in enacting RFRA, violated not only federalism but also separation of powers by intruding on the judicial function. Thus, the entire statute is invalid, not merely its application to the states. Indeed, the Seventh, Ninth and Tenth Circuits have reached this conclusion.[384] The Supreme Court nonetheless denied certiorari in *Young*, an Eighth Circuit case.[385] The outcome of this battle will obviously have far-reaching effects because it raises a core question regarding who is the final arbiter of the meaning of the Constitution and what is the scope of congressional power to expand on constitutional values.

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380. *Id.* at 859.

381. *Id.* at 861.

382. *Id.* at 863.

383. *See id.* at 861-62.

384. *See* Edward J.W. Blatnik, *No RFRAF Allowed: The Status of the Religious Freedom Restoration Act's Federal Application in the Wake of* City of Boerne v. Flores, 98 COLUM. L. REV. 1410, 1412-13 (1998) (listing cases diverging on whether RFRA is invalid only in its application to state law).

385. *See supra* note 375.

1998 SURVEY OF INDIANA CONTRACT AND BUSINESS LAW

JOSEPH R. ALBERTS*
JOHN W. HAMILTON**

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* Wooden & McLaughlin, Indianapolis. B.A., *cum laude*, departmental honors, 1991, Hanover College; J.D., *magna cum laude*, 1994, Indiana University School of Law.

** Wooden & McLaughlin, Indianapolis. B.A., Davidson University, 1986; J.D., *cum laude*, 1993, Washington & Lee University School of Law. The authors would also like to extend their thanks to Jeffrey A. Adams for his research assistance.

INTRODUCTION

This Article summarizes and comments upon selected appellate decisions during the survey period (November 1, 1997, to November 1, 1998)[1] in the areas of Indiana contract and business law. This Article does not include in-depth examination of decisions that, although they contain discussion about some contract principles or doctrine, are more appropriately addressed in the context of a survey of another area of substantive law, such as commercial law,[2] insurance law,[3] tort law,[4] real property law,[5] and business law.[6] Similarly, this

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1. This Article includes a few cases decided after November 1, 1998. In the interest of maintaining some semblance of brevity, this Article focuses only on federal and state appellate court decisions. There are, however, several published decisions from the United States District Courts in Indiana during the survey period that address and resolve important business and contract disputes. *See, e.g.*, Bridgestone/Firestone, Inc. v. Lockhart, 5 F. Supp. 2d 667 (S.D. Ind. 1998); Hayden v. Allstate Ins. Co., 5 F. Supp. 2d 649 (N.D. Ind. 1998); Seegers v. Pioneer Hi-Bred Int'l, Inc., 997 F. Supp. 1124 (N.D. Ind. 1998); Natare Corp. v. Aquatic Renovation Sys., Inc., 987 F. Supp. 695 (S.D. Ind. 1998); Deans v. Tutor Time Child Care Systems, Inc., 982 F. Supp. 1330 (S.D. Ind. 1998). In addition, the author's review of Indiana statutes found no significant revisions addressing contract and business law.

2. *See, e.g.*, Indiana-American Water Co. v. Town of Seelyville, 698 N.E.2d 1255 (Ind. Ct. App. 1998) (containing a helpful distinction between an indefinite quantities contract and a requirements contract).

3. *See, e.g.*, American Family Life Assurance Co. v. Russell, 700 N.E.2d 1174 (Ind. Ct. App. 1998) (interpreting an exclusion); Jones v. Western Reserve Group, 699 N.E.2d 711 (Ind. Ct. App. 1998) (interpreting policy language); Colonial Penn Ins. Co. v. Guzorek, 690 N.E.2d 664, 667-69 (Ind. 1997) (recognizing, inter alia, that contracts of insurance are governed by the same

Article does not include an in-depth analysis of those opinions issued during the survey period that apply quasi-contract doctrine.[7]

I. Survey of 1998 Indiana Contract Law

A. Contract Formation

1. Offer and Acceptance.—In *I.C.C. Protective Coatings, Inc. v. A.E. Staley Manufacturing Co.*,[8] I.C.C. Protective Coatings, Inc. ("I.C.C.") specialized in the application of paints, linings, and other types of protective coatings. A.E. Staley Manufacturing Co. ("Staley") manufactured various types of corn starches.

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rules of construction as are other contracts, that interpretation of an insurance policy is generally a question for the court, and that the power to interpret contracts does not extend to changing their terms); Hartford Accident & Indem. Co. v. Dana Corp., 690 N.E.2d 285, 294-96 (Ind. Ct. App. 1997) (utilizing contract principles in determining whether term "suit" in policy was ambiguous); Engelking v. Estate of Engelking II, 686 N.E.2d 932, 933 (Ind. Ct. App. 1997) (recognizing that an insurance policy is a contract and is subject to the same rules of interpretation as are other contracts) (citing Iemma v. Adventure RV Rentals, Inc., 632 N.E.2d 1178, 1182 (Ind. Ct. App. 1994)).

4. *See, e.g.*, Hagerman Const., Inc. v. Copeland, 697 N.E.2d 948, 962-63 (Ind. Ct. App. 1998) (dicta concerning whether a clause in an agreement purporting to provide indemnity for one of the parties' own negligence was ambiguous); CSX Transp., Inc. v. Kirby, 687 N.E.2d 611, 615 (Ind. Ct. App. 1997) ("'A party may not contract against his own negligence.'") (quoting Freigy v. Gargaro Co., 60 N.E.2d 288, 292 (1945)).

5. *See, e.g.*, Rothe v. Revco D.S., Inc., 148 F.3d 672 (7th Cir. 1998) (finding that a 1958 lease agreement did not require lessee's continuous occupation and use of premises as drugstore under doctrine of implied covenant); Dvorak v. Christ, 692 N.E.2d 920, 925 (Ind. Ct. App. 1998) (holding that an agreement to purchase a condominium unit was unambiguous); Beiger Heritage Corp. v. Montandon, 691 N.E.2d 1334, 1337 (Ind. Ct. App. 1998); (holding that a "due and payable" phrase used in lease agreement setting forth payment of real estate taxes was unambiguous and not intended to be used any differently from the way parties commonly have used the term in Indiana for decades); Nelson v. Marchand, 691 N.E.2d 1264, 1269-70 (Ind. Ct. App. 1998) (interpreting and applying a contract that included a warranty that construction of a home would be done in "good and workmanlike manner"); R.N. Thompson & Assocs. v. Wickes Lumber Co., 687 N.E.2d 617 (Ind. Ct. App. 1997) (discussing a purchaser's claim that the builder of a home breached the implied warranty of habitability).

6. Part II of this Article includes a substantive treatment of Indiana decisions and developments in the rather broad topic labeled "business law." One example of an Indiana decision containing language that may be helpful in a contract case although it is treated in detail in Part II of this Article under the rubric of "business law" is *Five Star Concrete, L.L.C. v. Klink, Inc.*, 693 N.E.2d 583 (Ind. Ct. App. 1998) (involving a lawsuit brought by a former member of a limited liability company against the company).

7. *See, e.g.*, Galanis v. Lyons & Truitt, 698 N.E.2d 368 (Ind. Ct. App. 1998) (applying quasi-contract *quantum meruit* principles in a case involving attorneys' fees).

8. 695 N.E.2d 1030 (Ind. Ct. App. 1998).

Staley sought bids from various companies for the application of a protective coating on the interior surfaces of three of its reactor tanks.[9] I.C.C. submitted a bid, which included a price, a list of specifications for the project, and a provision that I.C.C. retained the right to cure any defective work. I.C.C. sent a letter further detailing the bid, which stated the amount of time necessary to complete the contract, as well as travel, manpower, and equipment rates.[10]

Staley eventually awarded the contract to I.C.C. in a purchase order that provided in part:

> Provide labor & materials to line a total of three reactor tanks w/ceilcote Flakeline 103 matl. per specification outlined in your quotation . . . . All work to be performed using time and material rates outlined in your letter . . . . Staley to supply tank watch for confined space entry requirements. I.C.C. to supply monitoring and safety equipment for personnel in tank . . . .[11]

The purchase order also stated that the goods and services were to be purchased "in accordance with the terms of this purchase order, including those terms and conditions printed on the reverse hereof."[12] The terms on the order's reverse side provided that "any additional or different terms proposed by [I.C.C.] in any quotation, offer or otherwise are rejected unless expressly asserted in writing by Staley."[13]

I.C.C. signed and returned Staley's purchase order without objection, and began working on the project. I.C.C. purchased 480 gallons of the protective coating to cover all three tanks. After about a month, I.C.C. ceased work, having used 435 gallons while fully lining one tank and having applied only one coat to the second.[14] The day after I.C.C. ceased performance, Staley objected and arranged for an inspection of the work. The inspection revealed visible areas of materials embedded in the lining and that reactor surfaces were rough and jagged. In the opinion of a former employee of the coating liner, "I.C.C.'s work was the worst that he had ever seen and was far below industry standards."[15] At Staley's request, the former coating company employee sent I.C.C. a letter describing how to correct the defective work. I.C.C. sent Staley a letter indicating that I.C.C. would make all necessary arrangements to repair the work according to the manufacturer's specifications.[16] Despite I.C.C.'s letter, Staley canceled its

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9. Staley mixed various substances in the reactor tanks. Staley wanted to use a coating called "Flakeline 103" to avoid reactions between the steel in its reactors and caustic substances used in the manufacturing process. *See id.* at 1032-33.

10. *See id.* at 1033 & n.1.

11. *Id.* at 1033.

12. *Id.*

13. *Id.*

14. *See id.*

15. *Id.*

16. *See id.* at 1033-34.

purchase order the following day and contacted another company to correct the defective work.[17]

I.C.C. sued Staley for breach of contract and to foreclose on a mechanic's lien. Staley counterclaimed, asserting claims for, inter alia, breach of contract and breach of warranty. Both parties moved for summary judgment.[18] The trial court granted partial summary judgment to Staley, finding that the general terms and conditions, including the right to cure, had not been incorporated into the purchase order.[19] The case went to trial on the remaining counts, after which the trial court found for Staley.[20] I.C.C. appealed. The court of appeals affirmed.[21]

The court addressed two issues: (1) "[w]hether the trial court erred when it determined that I.C.C. did not have the right to cure under the parties' contract;" and (2) "[w]hether the trial court erred when it allowed testimony as to Staley's lost production and profits therefrom."[22]

With respect to the first issue, I.C.C. argued that Staley breached the contract when it refused I.C.C.'s offer to cure the defective work. "Specifically, I.C.C. argue[d] that its contract bid, which provided for the right to cure, formed the basis of the parties' agreement."[23] In the alternative, I.C.C. contended "that the bid was incorporated by reference into the parties' contract by operation of Staley's purchase order."[24] The court of appeals disagreed.[25]

The court of appeals resolved the "right to cure" issue as a matter of contract formation. The court did not need to decide whether I.C.C.'s bid was sufficiently detailed to constitute a formal offer.[26] Even assuming that it did, Staley's purchase order constituted a counteroffer because it varied the terms and conditions of the proposed agreement. The court pointed out that the purchase order reserved Staley's "right to reject, refuse or revoke any nonconforming goods ordered under the bid or to cancel any nonconforming performance."[27] The court also recognized that "[t]he order further stated that the remedies expressly provided by the purchase order were not exclusive of any other remedy allowed by law."[28] The court reasoned:

> Whether viewed as the original offer or as a counteroffer, the purchase

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17. *See id.* at 1034.

18. I.C.C.'s motion was for partial summary judgment; Staley's motion was for a summary judgment on all counts. *See id.* at 1032.

19. *See id.*

20. *See id.*

21. *Id.*

22. *Id.* For an in-depth analysis of the damages issues addressed and resolved by the court, see *infra* Part I.G.

23. *Id.* at 1034.

24. *Id.*

25. *Id.*

26. *Id.* at 1035.

27. *Id.*

28. *Id.*

> order was the offer which formed the basis of the parties' agreement. By signing and returning the purchase order, I.C.C. accepted the offer and, thus, entered into a binding agreement according to the terms and conditions set forth in the order. Absent a showing by I.C.C. that the parties did not intend the purchase order to be the sole memorial or integration of the contract . . . we must conclude that I.C.C. did not have the right to cure.[29]

Staley also argued that the purchase order contained an integration clause "confirm[ing] that the order was intended to be the sole memorial of the parties' agreement."[30] Indeed, the purchase order included a clause providing that "any additional or different terms proposed by [I.C.C.] in any quotation, offer or otherwise [is to be incorporated into this contract] . . . unless expressly asserted in writing by Staley."[31] The court agreed and, noting that the foregoing language was clear and unambiguous, concluded: "By signing Staley's purchase order without objection, I.C.C. obligated itself to the terms and conditions set forth in the order. Thus, we hold that the parties' contract was fully integrated and that we cannot consider parol evidence to determine whether I.C.C. had the right to cure."[32]

The court also disagreed with I.C.C.'s argument that its contract bid and subsequent letter to Staley were incorporated by reference into the purchase order. The court pointed out that the purchase order referred only to certain, specified sections of I.C.C.'s bid and letter.[33] The order specifically referred to the application process outlined in the bid and to the rates and time specifications outlined in the letter. Thus, according to the court, "the purchase order incorporated only those sections into the parties' agreement. All other sections, including the disputed right to cure, were not incorporated into the agreement."[34]

2. *Existence of Oral Contract.*—In *Creative Demos, Inc. v. Wal-Mart Stores, Inc.*,[35] Wal-Mart acquired several food stores owned by Wholesale Club, Inc. ("Wholesale Club") and afterward operated them under the Sam's Club trade name. Wholesale Club had hired Creative Demos to perform food

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29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.* at 1036.

33. *Id.*

34. *Id.* The *I.C.C.* court also disagreed with I.C.C.'s public policy argument that it was entitled to cure its performance deficiencies as a matter of the agreement. I.C.C. argued "that the opportunity to cure [was] a condition precedent for an action for breach of the implied warranty of fitness for habitation" and "that a right to cure was provided under the statutes controlling the sale of goods, automobiles, and health spas." *Id.* Citing Indiana's presumption that contracts represent the freely bargained agreements of parties and the public's interest not to restrict unnecessarily peoples' freedom of contract, the court determined that the right to cure, although recognized in several settings, is not guaranteed in every contract, regardless of the parties' actual agreement. *Id.*

35. 142 F.3d 367 (7th Cir. 1998).

demonstrations in the stores. In January 1991, a month before Wal-Mart took over, one of Wal-Mart's employees told Creative Demos that Wal-Mart would use its services through September 1991, after which Wal-Mart would conduct demonstrations in-house.[36] Wal-Mart replaced Creative Demos in March 1991, and thereafter Creative Demos filed suit. A jury awarded Creative Demos more than $7 million on their claim of early termination.[37]

On appeal, the Seventh Circuit Court of Appeals addressed the issues in four distinct areas: contract, promissory estoppel, fraud, and unjust enrichment.[38] This Article addresses in detail only the contract issue. In that regard, the Seventh Circuit agreed with the district court's decision to grant summary judgment to Wal-Mart on Creative Demos' claim that the Wal-Mart employee's statement created a contract for a definite term.[39] The court found crucial the fact that Wal-Mart and Creative Demos never reached agreement on issues such as whether Creative Demos' work could be terminated and for what cause.[40]

In another case involving an allegedly oral contract, *Lakes & Rivers Transfer v. Rudolph Robinson Steel Co.*,[41] the Rudolph Robinson Steel Company ("Robinson") entered into an agreement with Orion Maritime, Inc. ("Orion") "to ship some imported steel to the United States for sale to Robinson's customers in the Midwest."[42] A liner owned and operated by Orion was to ship the steel to Detroit and Chicago. Per the agreement, Robinson was to provide and pay for stevedores to unload cargo from the ship.[43] "The ship first docked at Detroit, where only a part of the steel bound for Detroit was unloaded. Orion then, on its own initiative, diverted the ship to Burns Harbor, Indiana, which was not one of its scheduled ports."[44] Stevedores unloaded the remainder of the cargo there.

Because Orion's diversion caused Robinson to incur additional expenses, Orion agreed to order and pay for the stevedoring services associated with the discharge of the cargo when the ship arrived at Burns Harbor.[45] While Robinson and Orion were negotiating that agreement, a Robinson employee called Lakes and Rivers Transfer ("Lakes & Rivers") to determine their rates for unloading so

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36. *See id.* at 368.

37. The district court reduced the award to $681,263. *See id.* at 369.

38. *Id.* at 369-73.

39. *Id.* at 369.

40. *Id.* With respect to the quasi-contract promissory estoppel issue, the jury concluded that Creative Demos was entitled to $681,126 because the Wal-Mart employee's statement caused Creative Demos to rely on an expectation of conducting demonstrations through September. *See id.* The award was the jury's estimate of lost profits. As the court pointed out, however, promissory estoppel does not support lost profits damages in Indiana. The court also took issue with whether the reliance worked to Creative Demos' detriment. *Id.*

41. 691 N.E.2d 1294 (Ind. Ct. App. 1998).

42. *Id.* at 1295.

43. *See id.*

44. *Id.*

45. *See id.*

that Robinson could decide whether Orion's offer would adequately defray its additional transportation expenses. During the telephone conversation, no one discussed who would pay for the services.[46]

Before the ship arrived at Burns Harbor, a local agent for Orion called Lakes & Rivers and indicated that the ship would be arriving shortly and needed to be unloaded quickly. The agent did not say who he was representing, but the Lakes & Rivers employee knew the agent and knew that he usually represented ship owners.[47] The day before the ship arrived, Lakes & Rivers sent a fax to Robinson, inquiring about who would be responsible for the stevedoring charges.[48] A week after the ship was unloaded, Lakes & Rivers again asked Robinson who would be responsible for the stevedoring costs. Robinson responded that Orion would be responsible.[49] After repeated unsuccessful attempts to collect from Orion, Lakes & Rivers demanded payment from Robinson.

Lakes & Rivers eventually sued Robinson, and on cross motions for summary judgment, the trial court granted summary judgment for Robinson.[50] Lakes & Rivers appealed, arguing that the parties entered into an oral contract that bound Robinson to pay for the stevedore services that Lakes & Rivers provided by virtue of Robinson's telephone inquiry about Lakes & Rivers' rates.[51]

The court of appeals affirmed the trial court's decision, recognizing first that a completed oral contract under Indiana law requires all parties to agree to all terms of the contract.[52] According to the appellate court, the parties did not agree on a crucial term of the alleged contract, namely "who was to pay for the services [Lakes & Rivers] was to provide."[53] Robinson's employee never represented to Lakes & Rivers, either orally or in writing, that Robinson was going to be responsible for the stevedore services. Rather, according to the court, "the evidence indicate[d] nothing more than that the [Lakes & Rivers] employee who spoke to the Robinson employee 'assumed' Robinson would pay, and assumed Orion was not responsible for the payment."[54] On those facts, the court was unwilling to hold that a mere inquiry about the price of a product or service, without more, creates a binding contract that obligates the inquiring party to purchase the product or service.[55] Thus, the court affirmed the trial court's

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46. *See id.*

47. *See id.*

48. *See id.*

49. Orion repeatedly acknowledged its responsibility to pay the stevedoring charges, but for reasons not discussed, Orion never paid. *See id.* at 1296.

50. *See id.*

51. *See id.*

52. *Id.*

53. *Id.*

54. *Id.*

55. *Id.* In addition, the court disagreed with Lakes & Rivers that Robinson was estopped

decision that the parties never reached an agreement on the terms and conditions alleged.

3. *Implied in Fact Contract.—Matter of J.W. v. Hendricks County Office of Family & Children*[56] marks Indiana's most recent published appellate decision with respect to implied in fact contracts. In *Matter of J.W.*, the Office of Family and Children ("OFC") filed a petition alleging that J.W. was a child in need of services due to his family's inability to adequately supervise him. The juvenile court placed temporary wardship with the OFC.[57] Among other things, the court ordered J.W.'s family to submit financial statements and insurance information to the OFC and to establish a child support account with the county clerk.[58] The family opened the account, filed a financial declaration, and provided the OFC case manager with insurance information.

Although J.W. initially stayed in his parents' home, OFC ultimately placed him with a private secure care facility. The juvenile court then entered a dispositional decree, ordering J.W.'s family to reimburse the OFC for placement costs.[59] After five months, J.W. returned home. The OFC petitioned the juvenile court for an order directing J.W.'s family to reimburse the OFC for J.W.'s total unpaid placement costs of $39,655.72. After a hearing, the juvenile court granted the motion.[60]

J.W.'s family appealed, raising two issues. The second of the two issues was whether an implied contract existed between the family and the OFC that obligated the OFC to place J.W. in a facility covered by the family's insurance.[61] According to J.W.'s family, the implied contract was created when they provided the OFC with insurance information and informed the case manager that their insurance policy required pre-approval for J.W.'s placement. They further claimed that the OFC breached the implied contract by placing J.W. in a facility not covered by their insurance.[62]

The court first set forth the requirements for an implied in fact contract in

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to deny the existence of a contract. The court pointed out that the evidence did not disclose any representation or concealment by Robinson that induced Lakes & Rivers to act to its detriment. According to the court, "[Lakes & Rivers] unloaded Robinson's cargo at the request of Orion's agent, without first determining who would be responsible for payment. When Robinson was finally asked by [Lakes & Rivers] who would pay for the stevedore services, Robinson responded that Orion was responsible." *Id.* at 1297. The court simply found no support for the suggestion that Lakes & Rivers would not have performed its services had it known Orion, and not Robinson, was responsible for payment. *Id.*

56. 697 N.E.2d 480 (Ind. Ct. App. 1998).

57. *See id.* at 481.

58. *See id.*

59. *See id.*

60. *See id.*

61. *See id.* at 484. The first issue was whether the juvenile court erred in ordering J.W.'s family to reimburse the OFC for the placement costs. *See id.* at 481-82.

62. *See id.* at 482.

Indiana:

> An implied in fact contract refers to the class of obligations which arises from mutual agreement and intent to promise, when the agreement and promise have simply not been expressed in words . . . . A contract implied in fact arises out of acts and conduct of the parties, coupled with a meeting of the minds and a clear intent of the parties in the agreement.[63]

Because there was no evidence of a mutual agreement between the parties and because the OFC did not manifest a clear intent to place J.W. in a facility covered by the family's insurance, the court of appeals refused to reverse the trial court and to imply a contract.[64]

B. Consideration

1. Unenforceable Promises.—In *In re Marriage of Arvin*,[65] the Arvins separated in 1996, at which time they reached a dissolution settlement. Craig Arvin was not represented by counsel. Kim Arvin's attorney drafted the settlement agreement. The trial court entered a decree of dissolution, which merged and incorporated the settlement agreement.[66] The settlement agreement provided for the settlement of all "issues attendant upon the dissolution of the marriage" and was agreed upon "in consideration of the mutual covenants contained herein."[67] The agreement also provided that the parties would have joint legal custody of the couple's two children and that the settlement agreement was made with the understanding that each party intended to remain in the Kokomo area to maintain the stability of the children. Another provision stated that no modification of the agreement would be valid unless in writing and executed by both parties.[68]

Immediately after the trial court entered the decree, Kim discharged her attorney, retained new counsel, and filed a motion requesting relief from the agreement. Kim argued that the agreement was entered into "without proper advice and without proper disclosure."[69] Kim then moved the children and herself over 100 miles from Kokomo to be with her new boyfriend and to obtain more suitable employment. She also filed a notice of intention to leave the

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63. *Id.* at 484 (citing McCart v. Chief Executive Officer in Charge, Indep. Fed. Credit Union, 652 N.E.2d 80, 85 (Ind. Ct. App. 1995)).

64. *Id.* at 484. The court also supported its decision by noting that the state has a compelling interest in protecting the welfare of children and advancing their best interests. In the case before it, the court pointed out that the OFC determined that it was in J.W.'s best interests to be placed in the facility they chose. *Id.*

65. 689 N.E.2d 1270 (Ind. Ct. App. 1998).

66. *See id.* at 1270-71.

67. *Id.* at 1272.

68. *See id.*

69. *Id.*

jurisdiction.[70] At that point, Craig filed a motion asking that the court require Kim to show cause why she should not be held in contempt for moving out of the Kokomo area in violation of the settlement/decree.

The parties ultimately tried all issues to the bench, after which the trial court denied Kim's motion to correct error but refused to hold her in contempt of court, finding that the move was "reasonable and further that she has provided to [Craig] extensive visitation with the children since the move."[71] Craig appealed, and the court of appeals reversed.[72]

On appeal, Kim argued that the covenant providing that the parties intended the children to remain in the Kokomo area was unenforceable because it was a vague recital of the parties' intentions and understandings. Kim also argued that the prohibition against modification was unenforceable because it violated public policy.[73] With respect to the second argument, the court agreed that the prohibition was most likely unenforceable, but the enforceability or the ability to modify the provision was insignificant under the circumstances because it was clear that Kim had no intention of honoring the covenant and instead immediately repudiated it.[74] According to the court, "[r]egardless of whether the covenant had been legally binding, it constituted sufficient consideration to support the parties' agreement regarding child custody such that [Kim] could not immediately repudiate the covenant without restoring [Craig's] rights to the status quo."[75]

With respect to the provision against moving the children, the court first recognized that even an unenforceable promise may constitute sufficient consideration to support a contract in Indiana.[76] The court then determined that the parties' covenant that they intended the children to remain in the Kokomo area to maintain their stability constituted sufficient consideration to support the agreement regarding child custody disposition.[77] Kim's immediate repudiation of her covenant constituted a failure of consideration with respect to the independent covenant of the agreement regarding child custody.[78] Because Kim made no attempt to return Craig to the status quo by relinquishing the benefit that accrued to her under the independent covenant (i.e., that she be awarded primary physical custody), the court reversed the trial court's decision with instructions that the child custody disposition in the agreement be held voidable at Craig's election and that the initial custody determination of the children be submitted

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70. *See id.*
71. *Id.*
72. *Id.* at 1274.
73. *See id.* at 1272-73.
74. *Id.* at 1273.
75. *Id.*
76. *Id.*
77. *Id.*
78. *See id.* at 1273-74.

for trial.[79]

2. *Independent Consideration for Unilateral Employment Contracts.*—Although the focus of the case was on the employment-at-will doctrine in Indiana, the Supreme Court of Indiana in *Orr v. Westminster Village North, Inc.*,[80] recognized in dicta that the court has yet to expressly address and resolve whether unilateral contracts in the employment context always require adequate independent consideration and whether an employee handbook can ever constitute a unilateral contract serving to modify the otherwise at-will employment relationship.[81] The *Orr* court expressly declined to use the case as a vehicle for resolving the issue.[82] Footnotes in the court's opinion reveal that decisions from the Indiana Court of Appeals on the issue are not "entirely clear and consistent,"[83] and that a number of decisions have held, "without discussing the adequate independent consideration requirement, that the terms of an employee handbook are irrelevant unless the employment contract is one for a definite term."[84]

C. *Enforceability of Exculpatory Clauses*

1. *Advertising Agreement.*—In *Trimble v. Ameritech Publishing, Inc.*,[85] an Ameritech advertising representative met with Trimble, a business owner who wanted to advertise in the Yellow Pages, to execute a written advertising order. The advertising contract Trimble signed provided "that any damages resulting from Ameritech's failure to publish the advertisement would be limited to the amount paid for the advertising or the contract price, whichever is the lesser."[86] The contract also contained the following exculpatory clause:

> *Publisher's liability*: . . . if publisher should be found liable for loss or damage due to a failure on the part of the publisher or its directory, in any respect, regardless of whether customer's claim is based on contract, tort, strict liability or otherwise, the liability shall be limited to an amount equal to the contract price for the disputed advertisements, or that sum of money actually paid by the customer toward the disputed advertisements, whichever sum shall be less, as liquidated damages and

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79. *Id.* at 1274.

80. 689 N.E.2d 712 (Ind. 1997).

81. *Id.* at 719.

82. *Id.*

83. *Id.* at 719 n.13 (comparing Tuthill Corp. v. Wolfe, 451 N.E.2d 72, 75, 78 (Ind. Ct. App. 1983) with Seco Chems., Inc. v. Stewart, 349 N.E.2d 733, 738 (Ind. App. 1976)).

84. *Id.* at 720 n.14 (citing Tri-City Comprehensive Community Mental Health Ctr., Inc. v. Franklin, 498 N.E.2d 1303, 1305-06 (Ind. Ct. App. 1986); Mead Johnson & Co. v. Oppenheimer, 458 N.E.2d 668, 671 (Ind. Ct. App. 1984); Campbell v. Eli Lilly & Co., 413 N.E.2d 1054, 1062 (Ind. Ct. App. 1980); Shaw v. S.S. Kresge Co., 328 N.E.2d 775, 778-79 (Ind. App. 1975)).

85. 700 N.E.2d 1128 (Ind. 1998).

86. *Id.*

> not as a penalty, and this liability shall be exclusive. In no event shall publisher be liable for any loss of customer's business, revenues, profits, the cost to the customer of other advertisements or any other special, incidental, consequential or punitive damages of any nature, or for any claim against the customer by a third party. . . .[87]

After Ameritech failed to publish Trimble's advertisement, Trimble filed suit seeking damages for loss of business resulting from the omission of advertisement. When Trimble filed suit, he had not been charged nor had he paid any money for the advertisement. The trial court granted summary judgment for Ameritech.[88] The court of appeals reversed.[89] The supreme court reversed the court of appeals, affirming the trial court's original decision to grant summary judgment and holding that exculpatory clauses such as Ameritech's are enforceable.[90]

The *Trimble* court first recognized the existence of two similar court of appeals cases, each of which involved Ameritech's previous failures to publish one of its customer's advertisements in the Yellow Pages: *Pigman v. Ameritech Publishing, Inc.*[91] and *Pinnacle Computer Services, Inc. v. Ameritech Publishing, Inc.*[92] The court in *Pigman* held that "the exculpatory clause contained in [Ameritech's] Yellow Pages advertising contract was unconscionable and void as against public policy as a matter of law."[93] The court in *Pinnacle* rejected *Pigman*, and held that "the exculpatory clause in Ameritech's Yellow Pages order was valid and enforceable."[94]

The *Trimble* court cites several cases recognizing parties' contractual freedom and the public's interest in not restricting that freedom unnecessarily.[95] The court also identifies five factors that courts and parties should consider when determining whether a contract that is not otherwise prohibited by statute nor tends to injure the public contravenes public policy:

> (1) the nature of the subject matter of the contract; (2) the strength of the public policy underlying any relevant statute; (3) the likelihood that refusal to enforce the bargain or term will further any such policy; (4) how serious or deserved would be the forfeiture suffered by the party attempting to enforce the bargain; and (5) the parties' relative bargaining

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87. *Id.* at 1128-29.
88. *See id.* at 1128.
89. *See id.*
90. *Id.*
91. 641 N.E.2d 1026 (Ind. Ct. App. 1994).
92. 642 N.E.2d 1011 (Ind. Ct. App. 1994).
93. *Pigman*, 641 N.E.2d at 1035.
94. *Pinnacle*, 642 N.E.2d at 1019.
95. *Trimble*, 700 N.E.2d at 1129 (citing Continental Basketball Ass'n v. Ellenstein Enters., Inc., 669 N.E.2d 134, 139 (Ind. 1996); Fresh Cut, Inc. v. Fazli, 650 N.E.2d 1126, 1129 (Ind. 1995); Weaver v. American Oil Co., 276 N.E.2d 144, 147 (Ind. 1971)).

power and freedom to contract.[96]

When applying the foregoing factors to the case at hand, the *Trimble* court pointed out that the second and third factors did not apply.[97] With respect to the other three factors, the court adopted the reasoning of the court of appeals in *Pinnacle* because the reasoning in that case "correctly resolves these considerations in favor of enforceability of the contract."[98] In so doing, the supreme court expressly rejected the decision in *Pigman*.[99]

2. Lease Agreement.—In *Vertucci v. NHP Management Co.*,[100] the Vertuccis rented an apartment in the Bent Tree apartment complex in Indianapolis. Before renting the apartment, Vertucci asked about security at the complex because his two teenage dâughters would be largely unsupervised during the day while he and his wife were at work. Employees assured him that there was security at the complex.[101] In addition, Bent Tree employees issued identification cards to every member of his family. Vertucci understood that the cards were to ensure that only tenants and their guests were using the common areas.

The lease agreement the Vertuccis signed contained the following provision:

> Tenant agrees that landlord, its employees, or agents shall not be liable for any damage or injury to Tenant, Tenant's family, agents, employees, or guests, or to any person entering the premises or the building of which the leased premises are a part, for injury to person or property arising from theft, vandalism, fire, or casualty occurring in the premises or the building. LANDLORD IS NOT RESPONSIBLE FOR, AND DOES NOT GUARANTEE, THE SAFETY OF TENANT, TENANT'S GUESTS, FAMILY, EMPLOYEES, AGENTS, OR INVITEES. TENANT AGREES TO LOOK SOLELY TO THE PUBLIC POLICE AUTHORITIES FOR SECURITY AND PROTECTION. ANY SECURITY THAT MAY BE PROVIDED IS SOLELY FOR THE PROTECTION OF LANDLORD'S PROPERTY. . . .[102]

After a non-resident sexually assaulted one of his daughters at the complex's swimming pool, Mr. Vertucci and his wife, as parents and natural guardians for their daughter, sued the complex's management company and related entities. The trial court granted the company's motion for summary judgment, which argued that it did not owe any duty to protect the Vertuccis from a third party criminal attack.[103]

The Vertuccis appealed. The court of appeals ultimately reversed the trial

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96. *Id.* at 1130.
97. *Id.*
98. *Id.*
99. *Id.*
100. 701 N.E.2d 604 (Ind. Ct. App. 1998).
101. *See id.* at 605.
102. *Id.* at 606 (emphasis in original).
103. *See id.* at 604.

court's decision with respect to whether the company owed such a duty.[104] In doing so, the *Vertucci* court first determined that the exculpatory clause in the company's lease did not prevent the company from having or assuming a duty to protect the Vertucci's daughter from the criminal actions of a third party.[105]

Although much of the court's opinion focuses on the negligence aspects of the case, the court first addressed the company's initial argument that the lease language quoted above effectively disclaimed its liability for injuries to tenants.[106] As the court wrote, the exculpatory clause in Bent Tree's lease form applied specifically to "*theft, vandalism, fire or casualty*."[107] The parties disagreed about whether the assault at issue was a "casualty" as interpreted by the lease, and the lease itself did not define the term.[108] To resolve the quandary, the court turned to Black's Law Dictionary, which defines "casualty" as "'[a] serious or fatal accident'" or a "'disastrous occurrence due to sudden, unexpected or unusual cause'" or an "'[a]ccident; misfortune; or mishap; that which comes by chance or without design[.]'"[109]

The court strictly construed the term "casualty" against Bent Tree, the lease's drafter, concluding that an intentional act such as that perpetrated against the Vertucci's daughter would not be considered a "casualty."[110] Accordingly, the court held that the exculpatory clause did not prevent Bent Tree from having or assuming a duty as the Vertuccis alleged.[111]

3. Health Club Membership Agreement.—In *Powell v. American Health Fitness Center of Fort Wayne, Inc.*,[112] Freda Powell signed a membership agreement to become a member at American Health's fitness center in Fort Wayne. The agreement contained the following exculpatory clause:

> 17. DAMAGES: By signing this agreement and using the Club's premises, facilities and equipment, Member expressly agrees that the Club will not be liable for any damages arising from personal injuries sustained by member or his guest(s) in, on, or about the Club, or as a result of using the Club's facilities and equipment. Member assumes full responsibility for any injuries, damages or losses which may occur to Member or their guest(s) in, on, or about the Club premises or as a result of using the Club's facilities and equipment. Member agrees that the Club shall not be liable for any loss or theft of personal property in or about the Club premises and does hereby fully and forever release and discharge the Club and all associated clubs, their owners, employees and

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104. *Id.* at 608.
105. *Id.* at 606.
106. *Id.*
107. *Id.*
108. *See id.*
109. *Id.* (quoting BLACK'S LAW DICTIONARY 218 (6th ed. 1990)).
110. *Id.*
111. *Id.*
112. 694 N.E.2d 757 (Ind. Ct. App. 1998).

> agents from any and all claims, demands, damages, rights of action, or causes of action present or future, whether the same be known or unknown, anticipated or unanticipated, resulting from or arising out of Member's or Member's guest(s) use or intended use of said Club premises, facilities or equipment.[113]

About a year later, Powell injured her foot while using a whirlpool at American Health's facility. She sued American Health, alleging that her injury was caused by its negligence. American Health filed a motion for summary judgment based upon the foregoing exculpatory clause. The trial court granted the motion, concluding that there was nothing ambiguous about the agreement, that Powell knowingly signed the agreement, and that, as a matter of law, Powell released American Health from liability for her claims.[114] Powell appealed, and the court of appeals reversed.[115]

The issue on appeal was whether the exculpatory clause in the contract released American Health from any liability for Powell's injuries sustained while on American Health's premises and caused by American Health's negligence.[116] Powell argued that the exculpatory clause was invalid because it was ambiguous. Specifically, Powell contended that the clause did not explicitly state that a member was releasing the health center from injuries resulting from the health center's own negligence. According to the court, Powell's argument was one of nonspecificity rather than ambiguity.[117] Citing *Indiana State Highway Commission v. Thomas*,[118] the *Powell* court recognized that the principle of specificity exists with regard to indemnity contracts and requires "an express stipulation as to the indemnitee's negligence" for the indemnity contract to be valid.[119] Recognizing the court's prior opinion in *Thomas*, the court held that an exculpatory clause intending to exculpate one party for liability because of its negligence to the other party must both specifically and explicitly refer to the negligence of the party seeking release from liability.[120]

As the court explained, American Health's exculpatory clause did not do so.[121] American Health's exculpatory clause provides that Powell released it from liability for "any damages" and placed the responsibility on Powell for "any injuries, damages or losses."[122] The clause also provided that Powell "fully and forever release[s] and discharge[s] [American Health] . . . from any and all claims, demands, damages, rights of action, or causes of action present or future

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113. *Id.* at 759.
114. *See id.*
115. *Id.* at 758.
116. *See id.*
117. *Id.* at 760.
118. 346 N.E.2d 252, 263 (Ind. App. 1976).
119. *Powell*, 694 N.E.2d at 760.
120. *Id.* at 761.
121. *Id.* at 760-62.
122. *Id.* at 761.

. . . resulting from or arising out of Member's . . . use . . . of said Club premises, facilities or equipment."[123]

According to the *Powell* court, such language never specifically or explicitly referred to the negligence of American Health.[124] Thus, the court held that, as a matter of law, the exculpatory clause did not release American Health from liability resulting from injuries sustained by Powell while on American Health's premises and caused by American Health's negligence, and that the clause was void to the extent that it purported to do so.[125]

D. Interpretation of Non-Exculpatory Contractual Terms

1. Employment Agreements.—The case of *Ruff v. Charter Behavioral Health System of Northwest Indiana, Inc.*,[126] is interesting in that it involves both a reformation theory and a dispute about contract terms. Ruff was a clinical psychologist and clinical director at a Charter facility in Michigan City. His employment contract provided that he receive a base salary plus 70% commission on all revenues from psychological testing he performed in excess of $15,000 per year.[127] After the facility in Michigan City closed, the facility's CEO, Michael Brown, offered Ruff the same position at a Charter facility in Hobart.

Ruff began working in Hobart without knowing what the terms of his employment would be. Brown eventually notified Ruff that Charter's central office had prepared a contract that Ruff needed to sign. "Ruff signed the contract without reading it."[128] The agreement provided that Ruff would receive an annual salary equal to what he received in Michigan City, but his 70% commission was based on testing in excess of $108,000 per year.[129]

Ruff's contract provided in relevant part:

> The term of this Agreement will be for one (1) year from August 5, 1996 and this Agreement will be self-renewing for additional one (1) year terms unless the Hospital or Psychologist terminates this Agreement as provided herein. Notwithstanding the preceding sentence, this

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123. *Id.*

124. *Id.* at 760.

125. *Id.* at 761-62. The court's opinion further explains that the clause was void even though other decisions from Indiana's appellate courts have upheld exculpatory clauses that have used similar language, *e.g.*, Shumate v. Lycan, 675 N.E.2d 749, 752 (Ind. Ct. App. 1997), Terry v. Indiana State Univ., 666 N.E.2d 87 (Ind. Ct. App. 1996); Marshall v. Blue Springs Corp., 641 N.E.2d 92, 95 (Ind. Ct. App. 1994). The *Powell* court determined that such decisions were distinguishable because the nonspecificity of the language used "was not put at issue nor addressed." *Powell*, 694 N.E.2d at 762.

126. 699 N.E.2d 1171 (Ind. Ct. App. 1998).

127. *See id.* at 1173.

128. *Id.*

129. *See id.*

> Agreement may be terminated by either party at any time, without cause, upon no less than sixty (60) days notice to the other party. If the Hospital terminates the Agreement, the Hospital may direct Psychologist to immediately cease providing services, although the Hospital will continue to be obligated to pay Psychologist those amounts due pursuant to Section 7 during the notice period.
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> * * *
>
> Psychologist shall receive and Hospital shall pay a base salary at the rate of ninety thousand dollars ($90,000) per year (the 'Base Salary'), payable in accordance with the Hospital's standard payroll policies.
>
> * * *
>
> Under the terms of this Agreement, Hospital will bill for, collect and retain all fees for Psychologist's services rendered to all patients treated by Psychologist, provided, however, that Hospital agrees to pay to Psychologist as additional compensation hereunder seventy percent (70%) of all net collections exceeding one hundred eight thousand dollars ($108,000) for Psychological testing. Psychologist shall not participate in any Hospital bonus plan. Upon the termination of this Agreement for any reason whatsoever, Hospital will continue to bill and collect on behalf of Psychologist, all of Psychologist's then outstanding accounts receivable from Psychologist's clinical practice at the Hospital for a period of one hundred eighty (180) days after such termination. Upon expiration of the Agreement, all uncollected accounts will be the property of the Hospital.[130]

Charter terminated Ruff approximately five months later. Ruff brought suit to reform the contract, claiming that Charter fraudulently induced him into signing the contract without reading it by representing that it was identical to his previous contract.[131] Ruff also sought a pro rata share of his commission based on psychological testing he performed in the five months before his termination. Both parties moved for summary judgment. The trial court denied Ruff's motion and granted Charter's, finding, inter alia, that Ruff had an opportunity to read the contract but chose not to and that Charter did not coerce or trick him into signing it.[132] The court of appeals reversed the trial court, holding that factual disputes remained with respect to both the reformation for fraud claim and the amount of commission claim.[133]

With respect to the reformation claim, the *Ruff* court pointed out that equity has jurisdiction in Indiana

> to reform written documents in only two well-defined situations: 1) where there is a mutual mistake— . . . where both parties mistakenly

130. *Id.* at 1175-76.

131. *See id.* at 1173.

132. *See id.*

133. *Id.* at 1176.

> execute a document that does not express the true terms of their agreement; or 2) where there has been a mistake by one party, accompanied by fraud or inequitable conduct by the remaining party with knowledge of the other's mistake.[134]

Apparently because the case involved the second of the two situations, the court's opinion initially spells out the elements of fraud in Indiana and ultimately concludes that whether Brown made a material misrepresentation of a past or existing fact, whether Ruff relied on Brown's representation, and whether Ruff was justified in doing so, were all questions of fact that precluded summary judgment.[135]

Next, the court addressed whether Ruff earned any commission pursuant to the contract's terms. Charter argued that Ruff is entitled to no additional compensation because "the commission due Ruff was figured and payable only when net collections exceeded $108,000."[136] Because Ruff did not work for Charter in Hobart until he had generated billing in that amount, he had not earned the commission. On the other hand, Ruff argued that the $108,000 figure was based on annual revenues for psychological testing and could be pro-rated monthly to figure the commissions he earned for the five months he was at Hobart.[137]

The *Ruff* court recited the familiar propositions that the intentions of parties to a contract are to be determined from the four corners of the document and that the test for determining the existence of an ambiguity is whether reasonably intelligent persons could come to different conclusions about the contract's meaning.[138] The court then pointed out that the contract Ruff signed did not mention how he was to earn his commission, thus, the contract was ambiguous on its face "as to how Ruff's commission was earned and was to be paid."[139] The court concluded that the trier of fact would need to hear extrinsic evidence concerning the intention of the parties to resolve the ambiguity.[140]

In *Eck & Associates, Inc. v. Alusuisse Flexible Packaging, Inc.*,[141] Eck and Alusuisse entered in to a contract whereby Eck would sell Alusuisse's product to Reflectix, Inc. in return for a 5% commission. The contract provided that it would continue indefinitely until terminated for just cause. Indeed, the relevant

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134. *Id.* at 1173.

135. *Id.* at 1174-75. Charter also argued that the parole evidence rule barred any evidence of oral representations about the contract. The court quickly pointed out, however, that an exception to the parol evidence rule applies in the case of fraud in the inducement. Because Ruff alleged fraud, the court reasoned that the parol evidence rule did not bar extrinsic evidence concerning the circumstances surrounding the execution of the employment agreement. *Id.* at 1175.

136. *Id.* at 1176.

137. *See id.*

138. *Id.*

139. *Id.*

140. *Id.*

141. 700 N.E.2d 1163 (Ind. Ct. App. 1998).

portions of the agreement provide as follows:

> 1. *Nature and Term of Service.* [Alusuisse] agrees to engage the broker [Eck] as an independent contractor and [Eck] agrees to act as Broker for [Alusuisse] in the business of selling products produced by Alusuisse . . . This agreement shall commence on the 4th day of August, 1989, and shall continue indefinitely, unless and until terminated by either party as hereinafter provided.
>
> 2. *Duties of Broker.* During the continuance of this agreement, the Broker shall devote such time as is necessary to the sale of the products of [Alusuisse], and shall use his best endeavors to promote its business and welfare. [Alusuisse] recognizes, in accordance with the Broker's regular business practice, he shall represent other firms and companies, but it is specifically understood that the Broker is in no event selling the products of, or representing companies which are in competition with, the products sold and manufactured by [Alusuisse]. . . .
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> * * *
>
> 8. *Termination—How Made.* This agreement may be terminated by either party *for just cause*, upon sixty (60) days written notice.
>
> 9. *Account.* [Eck] shall operate at, and sell only to Reflectix which is set forth on Exhibit "B".
>
> 10. *Nature of Relationship.* The relationship between the parties is that of a sales agent and independent contractor. [Eck] is authorized to accept an order on behalf of [Alusuisse]. To constitute a contract for sale, all orders taken by [Eck] must be duly acknowledged and accepted by [Alusuisse] at its respective authorized offices. Nothing contained in this agreement shall be construed as creating an employer/employee relationship between [Eck] and Alusuisse. [Alusuisse] will indemnify and hold harmless [Eck] against any and all claims for damages which may arise as a result of [Alusuisse's] products, plant or personnel.[142]

Conflicts arose among Eck, Reflectix, and Alusuisse that ultimately led Alusuisse to mail a notice to Eck terminating the contract.

Eck sued Alusuisse for breach of contract, alleging that Alusuisse lacked just cause for terminating the contract. Eck also sued Reflectix for interference with the contract. Reflectix filed a motion for summary judgment that Alusuisse joined. The trial court initially denied the motion, after which Eck and Reflectix settled their portion of Eck's claim.[143] Alusuisse renewed its motion for summary judgment, which the trial court granted, finding that the contract was

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142. *Id.* at 1167-68.

143. *See id.* at 1165.

terminable at-will.[144] The trial court never reached the question of whether Alusuisse had just cause to terminate the contract. The court of appeals reversed the trial court, holding that just cause of the broker's contract rebutted the presumption of an at-will employment and that separate and independent consideration was not a prerequisite to enforceability of the just cause provision.[145]

When addressing the substantive issues involved, the court of appeals began by recognizing the employment-at-will doctrine is a rule of contract construction, not a rule imposing substantive limitations on the parties' freedom to contract.[146] "If the parties include a clear job security provision in an employment contract, the presumption that the employment is at-will may be negated."[147] Additional facts revealed that Alusuisse traditionally cultivated broker relationships that were terminable at-will. However, Eck did not agree to a terminable at-will contract.[148] Instead, Eck submitted the modified contract for Alusuisse's approval. "Alusuisse opted to agree to the changes and signed the contract which contained a just cause termination provision, but lacked a unilateral-discretion-to-reassign-accounts provision."[149] As the court explained:

> Had Alusuisse intended the discretion which at-will termination affords, Alusuisse could have refused to deal with Eck. No assertion of unequal bargaining power was made. However, for reasons about which we may only speculate, Alusuisse chose to forego the at-will flexibility. The facts further reveal that once reminded of its unique contract with Eck, Alusuisse abided by its terms and did not try to terminate the contract until it arguably could demonstrate just cause.[150]

The court went on to hold that a job security provision does not need adequate independent consideration to rebut the at-will employment presumption.[151] In doing so, the court quoted extensively from *Streckfus v. Gardenside Terrace Co-op, Inc.*[152] In light of recent supreme court pronouncements making it clear that parties may rebut the presumption of employment at-will if they choose to include a clear job security provision in an employment contract,[153] and making it clear that parties' freedom to contract has continued to be highly valued, the *Eck* court saw no reason to require independent consideration for an explicit, freely bargained for and written just

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144. *See id.* at 1165-66.
145. *Id.* at 1169-70.
146. *Id.* at 1167.
147. *Id.*
148. *See id.* at 1168.
149. *Id.*
150. *Id.* at 1168-69.
151. *Id.* at 1169.
152. 504 N.E.2d 273, 275-76 (Ind. 1987).
153. *See* Orr v. Westminster Village N., Inc., 689 N.E.2d 712, 717 (Ind. 1997).

cause provision.[154]

In *Sample v. Kinser Insurance Agency, Inc.*,[155] the appellant-plaintiff, Cindy Sample ("Sample") worked for James Kinser ("Kinser") at the Kinser Insurance Agency ("Kinser Insurance"), an insurance agency based in Monroe County. Kinser authorized Sample to write policies for, among others, Erie Insurance Company. Kinser Insurance paid Sample on a commission basis, the terms and conditions of which were set forth in a written agreement as follows:

> 1. There will be a $400.00 minium [sic] commission payable monthly unless commissions are in excess of this, then the commission payment will be made vice the minimum.
>
> 2. A 75% commission on new business and renewal will be paid to a maximum period of one year and/or six months, depending on the volumn [sic] of business created. At a satisfactory amount of production agreed upon between Cindy Sample and James C. Kinser, the commission will then be reduced to Item #3 below. It is the intent of this agreement to help the agent achieve a level of personal monetary goals quickly and to help her maintain a productive salary until she gains time in the position and establishes a satisfactory renewal base of business.
>
> 3. After the goals of Item #1 and Item #2 are achieved and agreed upon, then Item #3 will take effect. This agreement changes the commission schedule to a 50/50 basis on new and renewal business with assignment to the Kinser Insurance Agency Inc. and all business will belong to the Corporation. The Kinser Insurance Agency Inc. will supply and pay all business cards, office expenses, and equipment as required to perform her duties as an agent of this Agency. Film, gas, and all vehicles expenses are to be supplied by the agent.[156]

Initially, Sample had binding authority to write policies for Erie as a sub-agent of Kinser Insurance. Subsequently, Kinser terminated that authority. Sample, relying on Kinser's representation, quit her job with Kinser Insurance.[157] Shortly thereafter, Kinser Insurance gave Sample a check that it contended

154. *Eck & Assocs.*, 700 N.E.2d at 1169. In reaching such a decision, the court specifically recognized the general principle that the at-will presumption applies to both oral and written employment contracts. Despite that recognition, the court distinguished the cases dealing with adequate independent consideration. Those cases, according to the court, were inapplicable, but not due to their lack of explicit, freely bargained-for just cause provisions. *Id.* Rather, the distinction was that they simply did not address the situation before the court. They involved employees arguing that some other consideration transformed what normally would have been an at-will employment situation into one that could only be terminated for just cause. *See id.*

155. 700 N.E.2d 802 (Ind. Ct. App. 1998).

156. *Id.* at 803.

157. *See id.*

represented the commissions Sample earned through the date on which she quit. Sample refused the check, contending that she also was entitled to receive commissions she had generated before termination, but that had not accrued until after her termination.[158] After the parties were unable to reach an agreement concerning the commissions, Sample sued Kinser and Kinser Insurance for breach of contract and for fraud. Kinser Insurance responded by filing a motion for summary judgment, which the trial court granted.[159] The trial court agreed that Sample was not entitled to receive commissions after her employment terminated.[160] The court of appeals reversed the trial court on the breach of contract claim and affirmed the trial court with respect to the fraud claim.[161]

The court of appeals noted that the contract Sample signed provided for commissions based on new and renewal business.[162] However, as counsel for Kinser Insurance correctly argued, the contract made no provision for commissions following her termination. Kinser Insurance also submitted the affidavit of Kinser, which stated "that the standard in the insurance industry is that commissions are not paid after a person leaves the employ of an insurance agency."[163]

Although the court conceded that industry standards may be important for some purposes, they were not relevant in this case:

> Although an employer and employee are free to agree that commissions will not be paid after the employee's termination, the general rule is that a person employed on a commission basis is entitled to those commissions when the order is accepted by the employer. . . . Stated differently a person employed on a commission basis is entitled to commissions on business she has secured even though payment is not received by the employer until a later date.[164]

Just because the agreement at issue in *Sample* was silent about whether Sample was entitled to commissions after her termination as an employee, did not, according to the court, mean that she is not entitled to commissions.[165] Rather, the court applied the foregoing rule. The court held that Sample was entitled to be paid commissions for renewal business she had secured before her termination.[166] According to the court, they were earned commissions; the sales had been consummated and Sample's right to the commissions had fully accrued,

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158. *See id.*
159. *See id.*
160. *See id.* at 804.
161. *Id.* at 802.
162. *Id.* at 804.
163. *Id.*
164. *Id.*
165. *Id.*
166. *Id.*

subject only to actual receipt of the premium payments.[167]

In *Haxton v. McClure Oil Corp.*,[168] Crystal Haxton ("Haxton"), was a cashier for McClure Oil Corporation ("McClure"). Haxton signed an employment agreement with McClure to work as a cashier. The agreement contained the following relevant terms:

> Term. The term of this agreement shall begin on October 19, 1995 and shall be an "at will" agreement. The Employee may terminate this agreement at any time by giving a required two weeks notice in writing. This notice is to be given to the Employee's immediate supervisor.
>
> * * *
>
> Conditions of Wage Reduction. The Employee agrees that their [sic] weekly paycheck can be reduced to the Federal Minimum wage rate if the following conditions exist:
>
> * * *
>
> Upon resignation, the Employee does not give the required written two weeks notice to their [sic] immediate supervisor.[169]

"On January 29, 1997, Haxton gave McClure a two-week written notice of her resignation. She quit working on February 2, 1997, four days after she gave notice."[170] McClure's last paycheck to Haxton compensated her for the hours she had worked and for one week's vacation. The amount McClure paid her, however, was based on the Federal Minimum Wage of $4.75 per hour rather than her hourly wage of $6.70 per hour.[171]

Haxton sued McClure in small claims court, seeking lost wages, statutory penalties, and attorney fees. After a trial, the court entered judgment against Haxton, determining that she had violated the terms of the employment agreement when she terminated her employment without working the full two weeks after she gave written notice.[172] Haxton appealed, citing two errors. The second of the two issues raised on appeal involved an interpretation of the employment agreement.[173] The court of appeals affirmed the trial court on that

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167. *Id.*

168. 697 N.E.2d 1277 (Ind. Ct. App. 1998).

169. *Id.* at 1279.

170. *Id.*

171. The total amount McClure paid Haxton was $459.11. Haxton was earning $6.70 per hour before she terminated her employment. *See id.*

172. *See id.*

173. The first issue was whether Haxton was entitled to her full rate of pay for the hours worked. *See id.* She contended on appeal that the employment agreement was an assignment of wages in violation of section 22-2-6-1 of the Indiana Code. She also argued that McClure, by reducing her pay assessed a fine against her in violation of section 22-2-81 of the Indiana Code. The court of appeals disagreed on both points, holding that both statutes were inapplicable. *Id.* at 1280.

issue.[174]

With respect to the allegedly ambiguous contract terminology, Haxton contended that she complied with the terms by giving two weeks written notice, even though she did not work the full two weeks. She claimed that she was entitled to be paid at her regular rate ($6.70 per hour), rather than at the minimum wage ($4.75 per hour) because the employment agreement was unclear as to whether she was required to work the full two weeks after her notice.[175] The court disagreed, concluding that the two-week notice provision in the employment agreement should be construed as requiring an employee to work for the period of his or her two-week notice.[176] According to the court, "[t]o hold otherwise would render the two-week notice element of the contract completely meaningless."[177]

In *Salin Bank & Trust Co. v. Review Board of Indiana Department of Workforce Development*,[178] Frances Hatfield ("Hatfield") worked for Salin in Columbus, Indiana in the bank's loan department when Salin decided to transfer the loan operations to Indianapolis. Hatfield chose to stay in Columbus until her position was eliminated. Hatfield understood that she was to receive compensation at the rate of one or two weeks' pay for each year of service up to a limit of twenty-six weeks of pay.[179] Hatfield signed what was, for lack of a better term, a termination agreement, which provided in part:

> Salin Bank and Trust Company agrees to pay you the total lump sum of $12,353.04, including all 1996 vacation, on the day following the 'Effective Date' of this Agreement, as that date is defined in paragraph 7.
>
> It is understood that this lump sum does not represent any moneys to which you are currently owed or have otherwise earned or accrued by the Effective Date pursuant to any compensation plans, practices, policies, programs or procedures. Payment of such earned or accrued moneys shall be made upon your request or when applicable, pursuant to the terms of any compensation plans, practices, policies, programs or

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174. *Id.*

175. *See id.*

176. *Id.*

177. *Id.* Although the court affirmed the trial court's disposition of the case with respect to the terms of the employment agreement, the court agreed with Haxton that McClure should not have reduced her vacation pay to the minimum wage level. The court equated vacation pay with a vested or accrued right where only the time of payment is deferred. Entitlement to vacation pay, according to the *Haxton* court, is not a gratuity but rather "is in the form of compensation for services." *Id.* at 1281 (citing Die & Mold, Inc. v. Western, 448 N.E.2d 44, 46 (Ind. Ct. App. 1983)). Absent an agreement to the contrary, the court concluded that Haxton should be entitled to the accrued vacation pay at the time of termination. Thus, the court remanded the issue to the trial court to compute and award Haxton the amount of her claim as it related solely to vacation pay. *Id.*

178. 698 N.E.2d 1 (Ind. Ct. App. 1998).

179. *See id.* at 2.

procedures.

> You agree to accept the above sum in full and final accord, satisfaction, compromise and settlement of any and all claims and rights, whether disputed or undisputed, accrued or unaccrued, liquidated or unliquidated, vested or nonvested, arising in any way out of or under your employment with Salin Bank and Trust Company . . . .[180]

Hatfield filed a claim with the Review Board of the Indiana Department of Workforce Development (the "Board") seeking unemployment compensation benefits, which were, of course, in addition to the lump sum payment Salin outlined in the termination agreement.[181] The Board awarded unemployment compensation benefits to Hatfield. Salin appealed, contending, inter alia, that the Board's decision contravened public policy because it failed to enforce a valid and unambiguous contractual agreement. The court of appeals disagreed, pointing out what it determined were ambiguities in the agreement.[182] First, the court recognized that although the agreement recites that the lump sum payment to Hatfield does not constitute "any moneys to which you are currently owed or have otherwise earned or accrued," the amount specifically includes payment of "all 1996 vacation."[183] Thus, the court agreed that "[a] clear ambiguity exists as to whether a portion of the lump sum payment is attributable to salary or other compensation owed to Hatfield."[184] The court pointed out another ambiguity by recognizing that the agreement specifically contemplated payment of other compensation even though it stated that the agreement constituted the full and final resolution of all matters arising out of the employment relationship.[185] The court concluded:

> [W]here the provisions of the agreement are ambiguous and Hatfield testified that she did not understand that the agreement intended to prevent her from filing a claim for unemployment compensation benefits, Salin cannot rely upon a public policy argument to enforce its intended purpose of the agreement.[186]

In *Schoemer v. Hanes & Associates, Inc.*,[187] Hanes & Associates ("Hanes") was the Indiana licensee of Dale Carnegie & Associates ("Carnegie"). Hanes offered various Carnegie courses on leadership and management. Hanes hired

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180. *See id.* at 2-3.

181. One of the issues resolved before the Board was whether Hatfield was laid off or whether she resigned her position. *See id.* at 4. The Administrative Law Judge found that she did not resign, but was laid off due to a lack of work, which is not a disqualifying condition for the denial of unemployment insurance in Indiana. *See id.* at 3-4.

182. *Id.* at 5.

183. *Id.*

184. *Id.*

185. *Id.*

186. *Id.*

187. 693 N.E.2d 1333 (Ind. Ct. App. 1998).

Schoemer as a training consultant under a contract that provided, in relevant part:

> The Training Consultant hereby acknowledges that he/she is an independent contractor for Hanes & Associates, Inc. . . .
>
> As an independent contractor, the Training Consultant:
>
> 1. Is paid strictly on commission;
> 2. Is considered self-employed, and therefore;
>   a. Will have no County, State or Federal Income taxes withheld and must fulfill this obligation himself/herself;
>   b. Will have no Social Security taxes withheld from his commission and must fulfill this obligation himself/herself;
>   c. Will have no State Disability Insurance (SDI) premium withheld from his commission;
>   d. Will have no unemployment insurance premium withheld; [and]
>   e. Is not covered by the Workers Compensation Act.
>
> 3. As an independent contractor, the association with Hanes & Associates, Inc. can be terminated at will by either party.[188]

Schoemer received commissions for "paid enrollments."[189] Any refunds were to be subtracted from Schoemer's next pay period. The employment contract also provided, in relevant part:

> In the event of termination, [Schoemer's] final check will be withheld until all outstanding leads, account files, office supplies, equipment, training material and/or selling aids are returned to [Hanes].
>
> In the event of termination, either voluntary or involuntary, [Schoemer] will be paid for all completed enrollments he/she has sold up to the date of termination. After that [Schoemer] will be paid only once more. The final pay will be made at the next regular end-of-the-month payday which is at least [thirty] days away from [Schoemer's] termination date. At the final payday, all completed enrollments will be paid for, as well as the appropriate commission rate on all money collected for pending enrollments, minus any 'buybacks,' cancellations, etc. After this final pay, the company will absorb any buybacks, cancellations, etc., normally charged to [Schoemer] and, likewise, will get credit for any future monies collected on [Hanes'] pending enrollments.
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> * * *
>
> If legal action is necessary to enforce the terms and conditions of this agreement, . . . [t]he prevailing party in any such action shall be entitled to recover all costs of suit and reasonable attorney's fees as determined

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188. *Id.* at 1336.
189. *Id.*

by the court.[190]

On November 18, 1993, Schoemer sold a customer relations training course to Citizen's Gas. Schoemer subsequently received a commission for the sale. On December 4, 1993, Hanes terminated its association with Schoemer, which Schoemer acknowledged on December 7, 1993.[191] Schoemer received his commission on December 21, 1993. However, in early January 1994, Citizen's Gas canceled its order and demanded a refund. Hanes immediately gave Citizen's Gas a refund and then demanded the commission from Schoemer.[192]

After Schoemer refused to return the commission, Hanes filed suit, seeking the reimbursement of the commission from Schoemer. The trial court entered judgment in favor of Hanes, including an award of attorney fees.[193] Schoemer filed a motion to reduce the judgment, which the trial court granted.[194] Both parties raised issues in the court of appeals.

Schoemer first argued that he was entitled to the statutory damages contemplated by Indiana Code section 22-2-5-1 for the alleged nonpayment of wages. The court disagreed, writing that relief available under section 22-2-5-1 of the Indiana Code is only available to employees and not independent contractors.[195] In this case, the court found that Schoemer was an independent contractor based on the language in the contract that provided that Schoemer was an independent contractor and would be paid strictly on commissions.[196]

Schoemer next argued that he was entitled to retain the commission paid with respect to the sale of training courses to Citizen's Gas. Again the court of appeals disagreed, holding that Schoemer was required to refund the commission.[197] The court reasoned that the terms of the contract stated that "[t]he final pay date will be made at the next regular end-of-the-month payday which is at least [thirty] days away from [Schoemer's] termination date."[198] Thus, because Citizen's Gas canceled its order and demanded a refund before Schoemer's final pay date, Schoemer was required under the contract to refund the commission to Hanes.[199]

2. *Purchase Agreements.—Francis v. Yates*[200] is a case in which the court of appeals addressed whether the right of first refusal contained in a contract for the

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190. *Id.* at 1336-37.
191. *See id.* at 1337.
192. *See id.*
193. *See id.*
194. *See id.*
195. *Id.* at 1338.
196. *Id.*
197. *Id.* at 1339.
198. *Id.*
199. *See id.* The court addressed whether Schoemer was entitled to additional compensation and Hanes' cross-appeal concerning their right to amend pleadings to conform to the evidence. *Id.* at 1339-40.
200. 700 N.E.2d 504 (Ind. Ct. App. 1998).

purchase and sale of real property violated the rule against perpetuities, thus rendering the contract void. Helen Yates ("Yates"), the owner of land in Bloomington, entered into a written agreement for the sale and purchase of such land with Donald Francis ("Francis"). The agreement described the three tracts of land to be sold and the purchase price. The terms of the agreement also gave Francis the option to purchase a fourth tract of land.[201] The details of the option were contained in a section of the agreement entitled "Option with Right of First Refusal to Purchase Real Property Part of Offer and Option to Purchase Real Property."[202] The option was effective for shortly over one year from the date of the execution of the agreement. The agreement contained a clause that provided:

> This option and the contract resulting from the exercise thereof shall bind and inure to the benefit of the heirs, administrators, executors, successors, and assigns of the respective parties. All rights of Purchaser hereunder may be assigned without restriction, but notice of each assignment shall be given in writing to Seller.[203]

Francis purchased the first three tracts in a timely manner. However, after over nine years had passed without Francis having exercised his option to purchase the fourth tract,[204] Yates sued Francis, seeking declaratory judgment that the right of first refusal violated the rule against perpetuities. Yates moved for summary judgment, which the trial court granted.[205] Francis appealed. The court of appeals reversed, concluding that fact issues concerning whether the term "option" referred to only the option provision or to the right of first refusal.[206]

On appeal, Francis conceded that the language extending the contract to the heirs, administrators, executors, successors, and assigns violated the common law Rule Against Perpetuities because his preemptive right to purchase the fourth tract attempted a non-donative transfer of a non-vested property interest.[207] Francis argued, however, that the extending language applied only to the option portion of the contract and not the right of first refusal.

After reciting well-settled Indiana law with respect to construction of written contracts,[208] the court recognized that the situation before it was one in which the

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201. *See id.* at 505.
202. *Id.* at 505.
203. *Id.*
204. *See id.*
205. *See id.*
206. *Id.* at 507.
207. *See id.* at 506.
208. Among the principles the court recognized were: (1) that the construction of written contracts are questions of law for which summary judgment is particularly appropriate; (2) that if ambiguity does not exist, then the court will not look beyond the four corners of the document to determine the parties' intent; (3) that specific words and phrases cannot be read exclusive of other contractual provisions; (4) that the parties intentions must be determined from the contract read in

agreement did not unequivocally include "extending language" applicable to the entire contract.[209] Rather, the applicable provision reads: "This option and the contract resulting from the exercise thereof shall bind an inure to the benefit of the heirs, administrators, executors, successors, and assigns of the respective parties."[210] From such language, it was not apparent to the court whether the parties intended the word "option" to refer to the option section of the agreement or if the parties intended the language to apply to both the option and right of first refusal.

Because the designated materials did not allow the court to determine the meaning of the term "option" as used in the agreement, the intent of the parties was unclear.[211] The court concluded that the contract was ambiguous and that the ambiguity could only be resolved by facts extrinsic to its four corners.[212] As such, summary judgment was inappropriate.

In *Salcedo v. Toepp*,[213] Dr. Salcedo contracted with Dr. Toepp to purchase his podiatry practice. The transaction was effected through four written contracts, including a Purchase Agreement, an Employment Agreement for Dr. Toepp, and a Lease Agreement. A fifth contract, a written Employment Agreement, was executed by Dr. Salcedo and Dr. Toepp's wife so that she could continue receiving health insurance through the practice.[214] Ultimately, litigation ensued on all of the contracts. A jury trial resulted in verdicts in favor of Dr. Salcedo on the Purchase Agreement, on Dr. Toepp's counterclaim on the Purchase Agreement, and on Ms. Toepp's claim under her Employment Agreement, and for Dr. Toepp on the Employment Agreement and on the Lease Agreement.[215] The trial court set aside the two verdicts for Dr. Salcedo on the Purchase Agreement and entered judgment on the remaining verdicts.[216] Dr. Salcedo appealed and the Toepps likewise raised several issues for cross-appeal. The court of appeals reversed and remanded with instructions that the trial court enter judgment on all of the jury's verdicts.[217]

Much of the appellate opinion concentrates on issues not germane to this Article.[218] However, the court's treatment of Ms. Toepp's claim under the

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its entirety; and (5) that courts strive to construe contractual provisions so as to harmonize the agreement. *Id.* at 506.

209. *Id.* at 507.

210. *Id.*

211. *Id.*

212. *Id.*

213. 696 N.E.2d 426 (Ind. Ct. App. 1998).

214. *See id.* at 428.

215. *See id.*

216. *See id.*

217. *Id.*

218. The first issue the court addressed involves the propriety of setting aside the verdicts for Dr. Salcedo under the Purchase Agreement. The issues addressed by the court on that issue are best left to substantive treatment as a labor/employment matter. *Id.* at 433-34. Similarly beyond the

Employment Agreement is interesting and worthy of a brief comment. Ms. Toepp's Employment Agreement read, in pertinent part:

> For all services rendered to [Dr. Salcedo] by [Ms. Toepp], [Dr. Salcedo] agrees to pay a gross monthly salary of Seven Hundred Dollars, less withholding and social security taxes. [Dr. Salcedo] will carry health and life insurance coverage on [Mrs. Salcedo] with the same coverage, terms and deductibles as is currently being carried by [Dr. Toepp]. . . .[219]

Ms. Toepp contended that because Dr. Salcedo owed her $7350 worth of wages under the Employment Agreement,[220] the jury's verdict in favor of Dr. Salcedo was contrary to law. In rejecting the argument, the court pointed out that the purpose of Ms. Toepp's Employment Agreement was to enable her to continue her health insurance through the practice. Thus, despite the plain language of the agreement, the parties never intended or expected that she perform any services for Dr. Salcedo. "Thus, the jury could reasonably have concluded that, just as Dr. Salcedo had waived his right to receive services from [Ms.] Toepp under the contract, [Ms.] Toepp had waived her right to compensation over and above the health insurance coverage that Dr. Salcedo provided through the practice."[221]

3. Settlement Agreements.—In *Silkey v. Investors Diversified Services, Inc.*,[222] the court of appeals affirmed the trial court's determination that an agreement between parties mediating a dispute was enforceable. The Silkeys sued Investors Diversified Services, Inc. and a broker named Mark Powers (collectively, "Brokers") for misrepresentation, violations of state securities law, breach of fiduciary duty, and constructive fraud, all stemming from investments that did not meet the Silkeys' expectations. The trial court ordered mediation, which resulted in an oral settlement agreement.[223] At the mediation, the mediator recorded a recitation of the terms of the agreement that his office later transcribed and forwarded to the parties. Counsel for the Brokers prepared a

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scope of this Article is the court's resolution of the adequacy of the damage award with respect to the Employment Agreement. *Id.* at 434.

219. *Id.* at 430.

220. The amount represented the agreed upon wage rate of $700 per month less amounts deducted for taxes and health insurance. *See id.* at 434.

221. *Id.* at 435. The court also resolved a dispute about entitlement to attorney fees. Indeed, both parties asserted that they were entitled to fees; Dr. Salcedo as a prevailing party under the Purchase Agreement and Dr. Toepp as the prevailing party under the Employment Agreement and the Lease Agreement for successfully defending against Dr. Salcedo's claim. *See id.* To resolve the matter, the court examined all three agreements, ultimately concluding that Dr. Salcedo was entitled to fees as the prevailing party under the Purchase Agreement and that Dr. Toepp was entitled to fees under the Lease Agreement. *Id.* at 436. Dr. Toepp, however, was not entitled to fees under the Employment Agreement. *See id.*

222. 690 N.E.2d 329 (Ind. Ct. App. 1997).

223. *See id.* at 331.

"Settlement Agreement and Mutual General Release" and sent it to the Silkeys for signature. The Silkeys refused to sign the written agreement and, thereafter, Brokers filed a "Motion to Enforce Mediation Agreement and Request for Sanctions."[224]

The trial court found as a matter of fact that the document accurately reflected the mediation agreement and that the Silkeys simply were attempting to repudiate the agreement.[225] The trial court also found that the audio tape recording was a legally binding form of the agreement that set forth with reasonable certainty the terms and conditions of the parties' agreement.[226] The trial court then directed that the terms of the audio tape recording be reduced to writing for signature of all parties.[227]

The investors appealed, and the court of appeals affirmed.[228] The central issue before the court of appeals was whether the oral agreement reached by the parties at the conclusion of the mediation was enforceable.[229] The Silkeys acknowledged that the parties reached an agreement at the mediation and that it was reduced to writing. However, they argued that they rescinded their verbal assent to the terms of the agreement and that the agreement was unenforceable because they neither signed it, nor filed it with the court.[230]

After an initial examination of the purposes of Indiana's Rules of Alternative Dispute Resolution ("ADR rules"), the court concluded that although the ADR rules control the process of mediation, "the enforcement of any valid agreement is within the authority of the trial court under the existing law in Indiana."[231] In response to the Silkeys' argument that they should not be held to an agreement about which they changed their minds, the court quickly recognized that such a rule "would clearly create a disincentive for settlement" and that it would "allow mediation to serve not as an aid to litigation, but as a separate and additional impetus for litigation."[232] The court concluded: "Having found that a settlement agreement had been reached, the trial court acted within its authority under the A.D.R. rules and the case law in Indiana in directing the parties to reduce their agreement to writing and sign and file it with the court."[233]

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224. *See id.*

225. *See id.*

226. *See id.*

227. *See id.*

228. *Id.*

229. *Id.* at 331-32.

230. *See id.* at 332.

231. *Id.*

232. *Id.* at 333.

233. *Id.* at 334. The court also rejected the Silkeys' argument that the agreement was not final or binding because it was oral and that it violated the Statute of Frauds. The court initially recognized that a settlement agreement in Indiana is not required to be in writing. *Id.* With respect to the Statute of Frauds issue, the court disagreed with the Silkeys' argument that the agreement could not be performed within one year of its making:

In *Indiana State Highway Commission v. Curtis*,[234] the Suttons owned real estate adjoining State Road 10 in Jasper County. In 1985, they granted the State of Indiana an easement for highway drainage work to be performed. In 1988, the Suttons sued the State and a contractor, alleging that the work had damaged their property and had resulted in an involuntary taking of their property.[235] Four days before trial, counsel for the State contacted counsel for the Suttons to discuss settlement and advised that a monetary settlement required the governor's approval, and that any easement over state property required Indiana Department of Transportation ("INDOT") approval. Ultimately, counsel arrived at an agreed amount for a monetary settlement from the State and the State's grant of an easement onto the State's property for the Suttons to install a new septic system. Counsel for the Suttons faxed a written agreement to counsel for the State, which he signed and returned.[236] Part of the agreement granted the Suttons access over State property, specifically: "[A]ccess through State Road 10's existing guardrail and any driveway therefrom as described in paragraph five (5) of this agreement is subject to approval by INDOT."[237]

After the State failed to deliver the money within the agreed forty-five days or to authorize installation of a septic system, the Suttons filed a motion to enforce the settlement agreement. The trial court found that the parties entered into a binding settlement agreement and granted the Suttons' motion to enforce the settlement. The trail court ordered the State to pay the settlement, permit the easement for the septic system, and pay attorney's fees to the Suttons.[238] The State appealed, and the court of appeals: (1) affirmed the trial court's enforcement of the agreement; (2) found sufficient evidence to demonstrate an agreement was reached; and (3) reversed the award of attorney's fees.[239]

The supreme court granted the State's petition to transfer and issued an opinion reversing the trial court's decision with respect to the enforcement of the agreement.[240] The supreme court first concluded that the agreement could not be held enforceable because the terms of the agreement required INDOT's approval of the easement provisions and there was no evidence in the record and no

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> It is possible that the agreement could be fully performed within one year of its making if the underlying investment were to pay a distribution equal to or greater than the guarantee amount within the first year. There is no express stipulation between the parties that the agreement would not be performed within one year.

Id.

234. 704 N.E.2d 1015 (Ind. 1998).
235. *See id.* at 1017.
236. *See id.*
237. *See id.*
238. *See id.*
239. Indiana State Highway Comm'n v. Curtis, 695 N.E.2d 143 (Ind. Ct. App. 1998).
240. The supreme court's opinion summarily affirms the court of appeals' decision with respect to attorney's fees. *Curtis*, 704 N.E.2d at 1020.

finding by the trial court to indicate that approval was given or waived.[241] The trial court had found that "'it is not equitable for the State to settle a case upon certain agreements . . . and then some eight months later repudiate the agreement.'"[242] The supreme court disagreed, writing:

> Failure to gain a required approval is not repudiation of the agreement. Rather it is insistence on compliance with the terms of the agreement. "The mere fact that a promise or condition is somewhat harsh or unfair in its operation is not enough to furnish such an excuse." . . . Because the condition—approval by the Governor and INDOT—is an essential part of the exchange and there is no evidence of extreme forfeiture or penalty the condition in this case is not excused. There are obvious public safety concerns involved in the granting of an easement that affects a safety rail on a public highway. It is quite reasonable that the contract required that INDOT approve such an arrangement, and that it be quite specific as to where and when and how rights under the easement are to be exercised.[243]

The supreme court recognized that even in non-public contracts, it is not uncommon for a settlement agreement to require approval by some agency or organization for one reason or another. Thus, the court concluded:

> [U]pholding the right of a party to insist on such a condition ultimately facilitates settlement by permitting an agreement to be made with an enforceable condition, even if the condition is likely to be fulfilled. Accordingly, as a matter of contract law, because INDOT approval was required by the settlement, and that approval was not obtained, the agreement, as to the easement provisions, is not enforceable.[244]

With respect to the second issue addressed, the *Curtis* court agreed with the State that the governor's approval is required for any compromise of a claim against the State:

> [I]n the area of tort claims we do have a separate body of law—the Tort Claims Act—that is applicable only to claims against governmental entities. . . . [O]nly the Governor has ultimate authority to compromise a claim. . . . Whatever its objective, the legislature is free to change that requirement, but unless and until this occurs, the Governor's approval is required before the State can compromise a tort claim.[245]

4. Loan Agreement.—In *Bastin v. First Indiana Bank*,[246] Janet Bastin

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241. *Id.* at 1018.
242. *Id.*
243. *Id.* at 1019.
244. *Id.* at 1019-20.
245. *Id.* at 1020.
246. 694 N.E.2d 740 (Ind. Ct. App. 1998).

("Bastin") obtained an adjustable rate mortgage loan from First Indiana in the amount of $23,750. The loan was evidenced by a note and had been serviced by First Indiana from its inception.[247] The note allowed First Indiana to adjust Bastin's interest rate on September 1 and March 1 of each year. Attached to the note was an Adjustable Rate Rider that provided, in relevant part:

> The interest rate that I will pay may change on the first day of March, 1985 and on that day every 6th month thereafter. Each date on which my interest rate could change is called an "Interest Change Date."
>
> * * *
>
> Beginning with the first Interest Change Date, my interest rate will be based on an Index. The "Index" is the weekly auction average rate for United States Treasury bills with a maturity of 6 months, as made available by the Federal Reserve Board. The most recent Index figure available as of the date 45 days before each Interest Change Date is called the "Current Index."
>
> * * *
>
> Before each Interest Change Date, the Note Holder will calculate my new interest rate by adding two and 25/100ths percentage points (2.25%) to the Current Index. The Note Holder will then round the result of this addition to the nearest one-eighth of one percentage point (.0125%). This rounded amount will be my new interest rate and will be effective on each Interest Change Date and will remain in effect until the next Interest Change Date.[248]

The sources of the rates are found in the Federal Reserve Board's issuance of the Statistical Release H.15, which is released each Monday. Other sources are *The Wall Street Journal* and an electronic service known as *Telerate*, which provides updated information daily.[249] When interest rates are rising, the borrower benefits from a bank's use of either the *Telerate* or *The Wall Street Journal*. When interest rates are falling, the buyer benefits from the H.15.[250]

"From the date of inception of Bastin's [n]ote until sometime in 1987, First Indiana relied on the index figure as published in *The Wall Street Journal*."[251] Subsequently, First Indiana began to obtain the index figure from the H.15 publication. First Indiana continued to provide Bastin with interest rate changes. "However, First Indiana never informed Bastin that it had switched from *The Wall Street Journal* to the H.15 publication as the source for the index figure."[252]

Bastin filed suit against First Indiana on behalf of herself and other similarly situated buyers, alleging that First Indiana charged excessive interest on its

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247. *See id.* at 742.

248. *Id.*

249. *See id.*

250. *See id.* at 742-43.

251. *Id.* at 743.

252. *Id.*

loans.[253] Bastin claimed that First Indiana breached the note because it was using the H.15 figure, which was not the most recent figure available. Bastin argued that the bank should have used *The Wall Street Journal* index. In the alternative, Bastin argued that even if use of the H.15 was proper, First Indiana still breached the note by previously using *The Wall Street Journal* as its source for the index figure.[254]

The trial court granted First Indiana's cross-motion for summary judgment and Bastin appealed.[255] The court of appeals held that the note was not ambiguous.[256] The fact that First Indiana interpreted the note differently by utilizing both the H.15 figure as well as *The Wall Street Journal* figure did not mean that the language in the note itself was ambiguous. The court reasoned that it is not bound by an erroneous interpretation placed on the contract by a party.[257] The fact that the note previously had been interpreted differently did not change its meaning.[258]

The court further wrote that the note's interest rate provision was subject to only one interpretation.[259] The word "index" as used in one part of the note was determined to be the same one as the "Current Index" used in the latter portion of the note.[260] The court reasoned that the note's language did not require First Indiana to use the index figure as published in *The Wall Street Journal* or as published by the *Telerate* method.[261] Rather, the "Current Index" or "Index" to be implemented by First Indiana was to be the "most recent index figure" that was "made available by the Federal Reserve Board."[262] Despite the availability of the weekly auction average through various secondary sources, the court agreed that the note clearly permitted First Indiana to use the index figure that was made available by the Federal Reserve Board.[263]

5. Agreement Between Spouses.—In *Pond v. Pond*,[264] the Supreme Court of Indiana addressed an interesting situation in which a husband and wife executed an agreement after the husband filed a petition for legal separation, but before the wife filed a petition for dissolution. The focus of the agreement was the division of marital property. The document recites that the parties were married at the time of the signing, that the husband had filed a petition for legal separation, and

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253. *See id.*
254. *See id.*
255. *See id.*
256. *Id.* at 747.
257. *Id.* at 745.
258. *See id.*
259. *Id.* at 746.
260. *See id.*
261. *Id.*
262. *Id.*
263. *Id.*
264. 700 N.E.2d 1130 (Ind. 1998).

that the husband would attend counseling sessions.[265] According to the agreement's terms, the husband's failure to attend counseling would void the agreement. Also part of the agreement was that the parties relinquished claims for temporary or permanent spousal support and all statutory inheritance rights. Finally, "the agreement include[d] a clause purporting to allocate certain attorney fees and contain[ed] a severability clause that declare[d] the remainder of the agreement to be enforceable if any portion [was] adjudged to be invalid, unlawful, or void."[266]

The attorney's fees clause provided: "In the event an attack by one party as to the validity of this agreement is unsuccessful, the party initiating such action shall be responsible for all attorney's fees and costs incurred by both parties in the prosecution or defense of such action."[267]

The trial court approved the parties' agreement except for the attorney's fees paragraph, which it held to be unconscionable.[268] Instead, the trial court ordered the husband to pay a substantial portion of the wife's attorney fees.[269] The court of appeals affirmed that decision without addressing whether the agreement was a reconciliation agreement, but reversed and remanded on other grounds.[270]

The Supreme Court of Indiana granted transfer and affirmed the trial court's decision to treat the agreement as a settlement agreement, but reversed the trial court's decision not to enforce the attorney's fees provision.[271] Before the supreme court, the husband contended that the agreement was a reconciliation agreement, which, he argued, the court should strictly enforce in the same manner as an antenuptial agreement. The wife countered that the agreement should be construed as a dissolution settlement agreement, which would allow the trial court to partially enforce or to modify it under Indiana Code section 31-1-11.5-10, part of the Indiana Dissolution of Marriage Act (the "Act").[272]

The supreme court found that the parties' agreement was not a reconciliation agreement and should not be treated as an antenuptial agreement.[273] Instead, the court pronounced that the agreement "clearly" fell within the ambit of the Act:

> This agreement was formed between the parties to a marriage, and its substance was directed at the amicable settlement of 'disputes that have arisen or may arise . . . attendant upon the dissolution of their marriage.' . . . The agreement was signed after the husband had commenced proceedings pursuant to the Act. The trial court did not err in construing

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265. *See id.* at 1134.
266. *Id.*
267. *Id.* at 1135-36.
268. *See id.* at 1134.
269. *See id.* at 1136.
270. Marriage of Pond, 676 N.E.2d 401, 408-09, 412-13 (Ind. Ct. App. 1997).
271. *Pond*, 700 N.E.2d at 1137.
272. *See id.* at 1132.
273. *Id.* at 1135.

the parties' agreement in accordance with the Act.[274]

With respect to the attorney's fees paragraph, the husband argued that the general principles of contract law require enforcement of the paragraph unless the contract is contrary to law or public policy. Although the court wrote that a contract for attorney fees is, as a general rule, enforceable according to its terms unless contrary to law or public policy, the court also pointed out that Indiana courts are not bound to accept every proffered settlement.[275] "In reviewing a settlement agreement, a court should concern itself only with fraud, duress, and other imperfections of consent, or with manifest inequities, particularly those deriving from great disparities in bargaining power."[276]

The trial court had refused to enforce the attorney's fees clause because it would have caused an economic impossibility to anyone but the husband to challenge the agreement, and because the court was concerned about the disparity of income between the parties.[277] According to the *Pond* court, such reasons "are insufficient to establish fraud, duress, other imperfections of consent, or manifest inequities."[278] Thus, the court reversed the trial court to the extent that the judgment of dissolution rejected and refused to enforce the attorney's fees clause.[279]

6. Construction Agreements.—In *Indiana Erectors, Inc. v. Trustees of Indiana University*,[280] the facts of the case were not disputed. In December of 1990, Indiana University (the "University") contracted with a general contractor, which general contractor contracted with a subcontractor ("SCI"), which subcontractor in turn entered into a subcontract with Indiana Erectors, Inc. ("Erectors") for the renovation of the Student Building on the Bloomington, Indiana campus. On December 17, 1990, employees of Erectors caused a fire that damaged the Student Building.[281] The University's general insurance carrier, the Allendale Mutual Insurance Company ("Allendale") paid the University approximately $1.9 million for the loss. No additional insurance policy had been obtained to cover the renovation of the Student Building and none of the contractors or subcontractors were specifically named as insureds in the Allendale policy.[282] Allendale brought an insurance subrogation action in the name of the University against Erectors, seeking damages under alternative

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274. *Id.*

275. *Id.* at 1136.

276. *Id.* (citing Voigt v. Voigt, 670 N.E.2d 1271, 1278 (Ind. 1996)). Citing *Voigt*, the court was quick to add that "the power to disapprove a settlement agreement must be exercised with great restraint. A trial judge should not reject such agreements just because she believes she could draft a better one." *Id.*

277. *See id.* at 1137.

278. *Id.*

279. *Id.*

280. 686 N.E.2d 878 (Ind. Ct. App. 1997).

281. *See id.* at 879.

282. *See id.*

theories of negligence and breach of the SCI/Erectors contract, of which the University was a third party beneficiary.[283] At trial, the jury returned a verdict in favor of the University in the amount of $1.9 million.[284] "The amount of the verdict/judgment reveals that the judgment was based on a breach of contract theory."[285]

The first issue addressed by the court was whether Erectors was an intended insured of the Allendale policy. Citing *LeMaster Steel Erectors, Inc. v. Reliance Insurance Co.*,[286] the court noted that when a party agrees to purchase insurance for the benefit of both parties to the contract, the first party in effect agrees to waive the intended insured's liability.[287] Thus, the first party would be precluded from bringing an action against the intended insured for any matter that was to be insured from, regardless of the fault of the intended insured.[288] Erectors asserted that it was entitled to judgment as a matter of law because it had been an intended insured under the interdependent, contractual relations between the University, its general contractor and the subcontractors. The trial court determined that Erectors was not an intended insured under the Allendale policy.[289] Accordingly, the trial court denied Erector's Motion for Summary Judgment.[290]

The trial court determined whether Erectors was an intended insured of the Allendale policy by reviewing the Construction Contract (the "Contract") between the University and its general contractor. Article 11 of the Contract governed insurance and stated that: "'Owner shall maintain during the course of construction, Builder's Risk Insurance . . . *The insured shall be the Owner and the Contractor(s) as their interests may appear* . . . .'"[291] Erectors argued that it was an intended insured as one of the "Contractors" involved in the project.

The court disagreed. In reviewing Article 4.1.1.2 of the Contract, the court noted that the term "Contractor" was defined as "all of the Prime Contractors, unless reference is made to the intended specific Prime Contractor."[292] Article 4.1.1.1. of the Contact identified the "Prime Contractors" as the "General

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283. *See id.* at 879-80.

284. *See id.* at 880.

285. *Id.* This proposition is based on the *Indiana Erectors* court's observation that the jury, in its verdict forms, "had reduced [the University's] recovery under its negligence theory by 25% (representing fault allocated to [the University]) producing a verdict in the amount of $1.425 million." *Id.*

286. 546 N.E.2d 313, 316-17 (Ind. Ct. App. 1989)

287. *Indiana Erectors*, 686 N.E.2d at 880.

288. *See LeMaster Steel Erectors*, 546 N.E.2d at 317.

289. *See Indiana Erectors*, 686 N.E.2d at 882.

290. *See id.* at 880.

291. *Id.* at 881 (quoting contract between the parties) (emphasis added by court). The Contract was a standard form construction contact. Article 11 of this form had been deleted and replaced with typewritten terms. *Id.*

292. *Id.*

Contractor," the "Mechanical Contractor" and the "Electrical Contractor."[293] This was significant, given that the University had hired a general, a mechanical, and an electrical contractor.[294] In addition, the court noted that the term "Subcontractor" was defined under Article 5.1.1. as "a person or entity who has a direct contract with the Contractor to perform any of the Work at the site."[295] Additionally, Article 5.2.4 provided that "nothing in this Contract shall create any contractual relation between any subcontractor and the Owner."[296]

Based on the above articles, the court concluded that the term "Contractor(s)" unambiguously referred only to the Prime Contractor, but did not include subcontractors.[297] The court then compared the case to *LeMaster*[298] in that under the unambiguous language of Article 11 of the Contract, the general contractor was an intended insured but the subcontractor was not. Thus, the insurance subrogation could properly proceed against the subcontractor.[299] Thus, the court affirmed the trial court's denial of Erector's motion for summary judgment.[300] Under the reasoning of the *LeMaster* case, the court refuted Erector's argument that its contract with SCI and SCI's subcontract with the general contractor gave rise to legitimate expectation on Erector's behalf that it was an intended insured under the University's construction contract. As in *LeMaster*, "[n]either [the] owner nor the owner's insurer can be bound by any subcontract to which neither was party."[301]

E. Repudiation/Mutual Mistake of Fact

In *Jay County Rural Electric Membership Corp. v. Wabash Valley Power Ass'n*,[302] Jay County Rural Electric Membership Corp. ("Jay County"), a rural electric membership corporation that purchased wholesale electricity for

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293. *Id.*

294. Paragraph 4.1.1.1. provides "the work of this Project has been divided into the following parts, for which there will be separate, prime contractors as indicated below: 1) General Construction work, by the General Contractor, 2) Mechanical Construction work, by the Mechanical Contractor, 3) Electrical Construction work by the Electrical Contractor and 4) Other." *Id.*

295. *Id.*

296. *Id.*

297. *Id.*

298. LeMaster Steel Erectors, Inc. v. Reliance Ins. Co., 546 N.E.2d 313, 317-20 (Ind. Ct. App. 1989).

299. *See Indiana Erectors*, 686 N.E.2d at 881. The court noted that because Article 11 of the standard construction contract had been revised, the court's holding in *South Tippecanoe School Building Corp. v. Shambaugh & Son, Inc.*, 395 N.E.2d 320 (1979), where the court held that the subcontractor was an intended beneficiary under the construction contract, was inapplicable. *Indiana Erectors*, 686 N.E.2d at 881-82.

300. *Indiana Erectors*, 686 N.E.2d at 882.

301. *Id.*

302. 692 N.E.2d 905 (Ind. Ct. App. 1998).

distribution, sued the Wabash Valley Power Association ("WVPA"), an electric generation and transmission cooperative, as well as the Kosciusko County REMC. In 1977, Jay County became a member of the WVPA by signing an all-requirements wholesale power supply contract. The contract required Jay County to purchase all of its power and energy requirements for its system from WVPA.[303]

In December of 1996, Jay County sent notices purporting to withdraw its membership in the WVPA and to terminate the all-requirements contract with WVPA. Jay County then filed suit against the WVPA, seeking that the trial court declare its withdrawal and termination valid.[304] "It also negotiated a contract with Cinergy that would guarantee better prices for electricity."[305] WVPA moved for a temporary restraining order and preliminary injunction to require Jay County to purchase its electricity exclusively from WVPA during the pendency of the litigation. The trial court issued the injunction, and Jay County timely initiated an interlocutory appeal.[306]

When determining whether the trial court erred in issuing the injunction, one of the factors the *Jay County* court examined was the likelihood of success at trial.[307] In that context, Jay County offered three arguments in support of its contention that it likely would have succeeded at trial, the first two of which were anticipatory repudiation and mutual mistake.[308] Jay County first argued that WVPA repudiated its contract when it notified Jay County of its desire to merge with another cooperative, Hoosier Energy. On that issue, the trial court found that WVPA began having conversations with Hoosier Energy in late 1996 about the possibility of merger.[309] In February 1997, Jay County was informed that WVPA and Hoosier Energy would consider merger at their February board meetings. Before the board meetings, Jay County decided to formally terminate its corporate and contractual relationship with WVPA.

The trial court, therefore, concluded that at the time Jay County treated the all-requirements contract as terminated, WVPA had not communicated a positive, absolute, and unconditional repudiation of the contract, and ultimately concluded that there was a likelihood that WVPA would prevail at trial on this issue.[310] According to the court of appeals:

> The trial court was well within its discretion in so concluding, as questions remain as to whether (1) Jay County prematurely reacted to WVPA's preliminary statements of intent to merge; (2) whether a merger

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303. *See id.* at 908.
304. *See id.*
305. *Id.*
306. *See id.* at 907.
307. *Id.* at 909.
308. *See id.* at 910. Jay County also argued that the WVPA failed to comply with statutory preconditions for conducting business. *Id.* The third factor is beyond the scope of this Article.
309. *See id.* at 911.
310. *See id.*

> would actually constitute a repudiation of the all-requirements contract; and (3) whether Jay County read 'repudiation' into WVPA's intentions because it wanted out of the contract in order to preserve its more favorable contract with Cinergy.[311]

The *Jay County* court next turned its attention to Jay County's mistake of fact argument. "Jay County argue[d] that a material feature of the all-requirements contract was both parties' understanding that WVPA's involvement in [the Marble Hill nuclear power facility] would result in more reliable and economical power, an understanding that constituted a mutual mistake."[312] On that issue, the trial court found that, at the time it entered into the contract, the Jay County Board understood that the contract was a long-term commitment that obligated Jay County to purchase its total requirements from WVPA regardless of whether WVPA ever received power from Marble Hill.[313] The trial court also found that the investment in Marble Hill, like many investments, was risky and that the doctrine of mutual mistake did not apply.[314] Thus, the trial court concluded that there was a likelihood that WVPA would prevail at trial.[315] In affirming that decision, the court of appeals simply held that "the [trial] court's conclusions were well within its discretion."[316]

F. Rescission

1. Rescission for Fraud.—In *Drudge v. Brandt*,[317] Louise Drudge ("Drudge") sued her daughter, Jean Brandt ("Brandt") for alleged breach of contract and constructive fraud. The dispute arouse out of two separate events. First, Drudge advanced to Brandt approximately $50,000 so that Brandt could buy a new home in Indiana. Drudge contended that she advanced the funds with the understanding that Brandt would pay her back when Brandt's home in Florida sold.[318] A few months later, Drudge agreed to transfer money into an annuity that was placed in Brandt's name. In exchange, Brandt agreed to pay the interest income on the annuity to Dredge. According to Drudge, Brandt did not repay the advancement even after she sold her Florida home and Brandt failed to pay her the interest income from the annuity as promised. As a result, "Drudge claimed that Brandt's actions constituted a breach of contract as well as constructive

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311. *Id.* The court also addressed Jay County's argument that the trial court erred in determining that WVPA provided the "adequate assurance of performance" required by section 26-1-2-609 of the Indiana Code. *Id.* Because that issue is more appropriately addressed in the commercial law survey, it is beyond the scope of full treatment here.

312. *Id.* at 912.

313. *See id.*

314. *See id.*

315. *See id.* at 911.

316. *Id.* at 912.

317. 698 N.E.2d 1245 (Ind. Ct. App. 1998).

318. *See id.* at 1246.

fraud."[319]

Brandt denied that she took advantage of Drudge. She admitted that Drudge had given her money to buy her home in Indiana and that she originally agreed to repay Drudge when she sold her house in Florida, but claimed that the parties later modified the agreement.[320] Brandt also "denied that there was any agreement to pay the interest income from the annuity to Drudge."[321]

The trial court entered judgment for Drudge, declaring that all interest payments on the annuity were for Drudge's benefit and could be paid directly to her, but refusing to allow Drudge to rescind the agreement and recover the principal amount of the annuity.[322] The first of the two issues Drudge appealed was whether the trial court erred in failing to order that the agreement pertaining to the annuity be rescinded and the annuity transferred to her.[323] Drudge relied on three cases in support of her position, *Dowell v. Jolly*,[324] *Tibbetts v. Krall*,[325] and *Cree v. Sherfy*.[326] All three "cases involv[ed] aged or infirm persons who transferred land to others in exchange for an agreement to provide care and maintenance during the transferor's lifetime."[327]

The *Drudge* court was not persuaded by the foregoing cases, concluding that they did not compel rescission of the agreement.[328] The court reasoned and concluded:

> First, the property transferred in this case was not land. Rather, it was money used to purchase an annuity in Brandt's name. Second, the transfers of land in the earlier cases were in exchange for agreements to provide personal services to the transferor, and not merely the repayment of accrued interest on an annuity. Because of the unique character of both land and the provision of personal care and maintenance to an aged and infirm person as consideration for the transfer of such property, rescission as the only practical remedy to be afforded in the event of a breach. . . . Here, neither the property conveyed, i.e., money with which to purchase an annuity, nor the property promised in exchange, i.e., the accrued interest on the annuity during Drudge's lifetime, were unique.

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319. *Id.*

320. *See id.* at 1247.

321. *Id.*

322. *See id.* at 1249. The trial court also refused to impose a constructive trust. *See id.* at 1250.

323. *See id.* at 1248-49. The second issue the court of appeals addressed was whether the trial court erred in not finding that Brandt had committed constructive fraud and in not ordering that the annuity be placed in a constructive trust. The court of appeals affirmed on both issues. *Id.* at 1249-50, 1250.

324. 159 N.E.2d 590 (Ind. App. 1959).

325. 145 N.E.2d 577 (Ind. App. 1957).

326. 37 N.E. 787 (Ind. 1894).

327. *Drudge*, 698 N.E.2d at 1249.

328. *Id.*

> Under the circumstances presented in this case, we cannot say that the judgment entered by the trial court is contrary to law or that the trial court erred in failing to grant a rescission of the contract.[329]

2. Rescission for Failure to Meet Conditions Precedent and Subsequent.—In *Barrington Management Co. v. Paul E. Draper Family, Ltd. Partnership*,[330] the parties entered into a written Purchase Agreement under which Draper agreed to sell a parcel of commercial real estate to Barrington. The Purchase Agreement provided that "[t]ime is of the essence of this Contract" and an Addendum also noted that "[t]ime is important."[331] The closing was to take place after all conditions had been satisfied or waived. The Addendum also provided that a condition of the offer was that utilities, city water, electric, gas, and storm drainage were available to the property line and were in adequate supply and capacity to serve the development. The agreement gave the purchaser 180 days from the date of the agreement to satisfy or waive the condition.[332]

Barrington experienced delays in satisfying the condition because it had problems obtaining the land use and drainage approvals necessary to develop the property. The parties agreed to extend the period in which Barrington could satisfy or waive the condition. Barrington requested a second extension, but Draper refused.[333] Barrington then demanded that Draper close the transaction and forward the closing documents. Draper refused to close and filed suit, requesting that the Purchase Agreement be rescinded to enable it to sell the real estate to another purchaser. Barrington counterclaimed, requesting specific performance.[334] The parties agreed to disposition by "summary proceedings," after which the trial court entered judgment in Draper's favor, thereby granting rescission of the Purchase Agreement and that Draper could retain the earnest money deposit.[335] Barrington appealed.

On appeal, Barrington argued that Draper breached the Purchase Agreement by refusing to close the transaction and that the trial court erred by considering parol evidence on the issue of whether the land use and drainage approvals were a condition constituting a material part of the consideration benefitting Draper that could not be waived.[336] The court of appeals disagreed, pointing out that it could affirm the trial court's judgment notwithstanding consideration of parol evidence because the trial court also found that Draper was entitled to rescind the Purchase Agreement upon the failure of a condition subsequent (the expiration of the time allotted for Barrington to satisfy or waive the condition regarding the

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329. *Id.* at 1250.
330. 695 N.E.2d 135 (Ind. Ct. App. 1998).
331. *Id.* at 138.
332. *See id.* at 142.
333. *See id.* at 139.
334. *See id.*
335. *See id.*
336. *See id.* at 141.

procurement of land use and drainage approvals).[337] Citing favorably both the "time of the essence" provisions in the Purchase Agreement and *Dvorak v. Christ*,[338] the court held that the Purchase Agreement became legally defunct once the time period of the parties' first extension expired.[339] Thus, the trial court did not abuse its equitable discretion when it granted Draper's request for rescission.[340]

Because Indiana law requires that the party seeking rescission of a contract must return the defaulting party to the status quo, the court of appeals determined that Draper had to return the earnest money paid under the contract.[341] Accordingly, the court reversed that portion of the trial court's decision allowing Draper to retain the earnest money.[342]

G. Breach/Damages

Judge Staton's opinion in *Bee Window, Inc. v. Stough Enterprises, Inc.*[343] addresses a single issue under Indiana law: Whether a party breached a written services contract. Bee Window entered into an agreement with Stough Enterprises, the management corporation for Indianapolis Blood Plasma, Inc. (collectively, "Stough"), whereby Bee Window would furnish and install twenty-three windows and perform incidental work at the Blood Plasma building located on North Capitol Avenue in Indianapolis.[344]

Bee Window fabricated the windows on site using raw materials including lumber, glass, and vinyl framing material received from a supplier. The vinyl material proved unsuitable. "[T]he windows rattled, leaked, and deflected inward and outward up to seven inches during windstorms."[345] Stough complained to Bee Window and withheld final payment. Bee Window failed to cure the problem and Stough sued Bee Window for breach of contract.[346] After a bench trial, the trial judge awarded Stough damages and denied Bee Window's motion to correct error. Bee Window appealed.[347] The court of appeals affirmed.[348]

The first of the two issues Bee Window raised was whether the trial court's

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337. *Id.*

338. 692 N.E.2d 920, 924 (Ind. Ct. App. 1998). *See supra* note 6 and accompanying text.

339. *Barrington Management*, 695 N.E.2d at 141.

340. *See id.* at 142.

341. *Id.*

342. *Id.* The court next addressed the issue of attorneys fees, *id.* at 142-43, this Article does not address this issue in detail.

343. 698 N.E.2d 328 (Ind. Ct. App. 1998).

344. *See id.* at 329.

345. *Id.*

346. *See id.*

347. *See id.*

348. *Id.*

determination that Bee Window breached its contract was clearly erroneous.[349] With respect to that issue, Bee Window relied on the case of *Millner v. Mumbry*,[350] a case in which the plaintiff, who claimed to be an engineer, developed his own plans and specifications for a "berm house."[351] Those specifications were written into the agreement and the defendant, a concrete contractor, poured concrete walls in accordance with the plaintiff's plans. After completion of the house, the walls began to develop cracks and the plaintiff sued. The *Millner* trial court found for the contractor and the court of appeals affirmed because it would not require the contractor to pay for doing exactly what the plaintiff required.[352]

The *Bee Window* court distinguished *Millner* on its facts because Stough did not supply the specifications for constructing the windows.[353] "Stough specified only that [they] retain an aesthetic vertical and horizontal pattern."[354] The court concluded:

> In this case, the parties agreed that Bee Window would provide windows for twenty-three openings. Inherent in that agreement was an understanding that the windows would function as windows. Yet the record indicates they leaked rain, deflected inward and outward with changes in air pressure, failed to meet building code regulations and, more compelling, created a serious threat to life because they could explode or implode into razor-sharp pieces of glass. The trial court's ruling that Bee Window breached its contract with Stough is not clearly erroneous.[355]

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349. The second of the two issues on appeal concerned whether the $45,615 damage award was within the scope of the evidence. *See id.* On that issue, the *Bee Window* court could not agree that the conclusion was erroneous. *Id.* at 330-31. The trial court arrived at the damage award by subtracting the amount Stough initially refused to pay Bee Window for the original work from the lowest bid to remove and replace the window system. The trial court concluded that the existing windows Bee Window installed had no value and, in fact, subjected Stough to "'the threat of tremendous tort liability[.]'" *Id.* at 330-31 (quoting the trial court).

350. 599 N.E.2d 627 (Ind. Ct. App. 1992).

351. According to the *Bee Window* court's description, a "berm house" is a structure built into embanked earth. *Bee Window*, 698 N.E.2d at 330.

352. *See id.*

353. *Id.*

354. *Id.* Bee Window recommended a vinyl window frame that would perform better than aluminum. Bee Window also contended that it installed the windows in conformance with specific design specifications provided by a third party supplier/manufacturer and agreed to by Stough. *See id.* The court of appeals wrote that the trial court was free to accept or reject Bee Window's testimony regarding the existence and compliance with a specific design. In either event, the court of appeals concluded, "Stough did not develop technical expertise." *Id.*

355. *Id.*

In *Holloway v. Bob Evans Farms, Inc.*,[356] Dorothy Holloway ("Holloway") sued Bob Evans Farms, Inc. ("Bob Evans") and Norpac Foods, Inc. ("Norpac") in negligence and breach of contract after finding a worm in her meal while eating at a Bob Evans restaurant. Norpac supplied the frozen vegetables in which the worm was allegedly found. The trial court granted both Bob Evans's and Norpac's motions for summary judgment.[357] The court of appeals reversed in part and affirmed in part.[358]

The first issue the court of appeals addressed was a procedural one: Whether Holloway's complaint sufficiently asserted a breach of contract claim under Indiana's notice pleading practice.[359] Count I of Holloway's complaint provided in relevant part:

> 9. Bob Evans knowingly invited [Holloway] into its restaurant and expressly offered by its menu and staff to prepare and deliver to [Holloway] wholesome food in return for a price set by which [she] agreed to pay.
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> 10. Norpac knowingly delivered frozen food products to Bob Evans with the intention that the same be prepared and sold to the public who were invitees to Bob Evans.
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> 11. Bob Evans recklessly and negligently failed to exercise reasonable care in the preparation of the food ordered by [Holloway], and Norpac negligently packaged the food products sold to [her].
>
> 12. As a direct and proximate result of [bob Evans's and Norpac's] negligence and failure to exercise reasonable care, [Holloway] suffered injury to her person of a continuing nature and out-of-pocket losses as hereinabove set forth.[360]

According to the *Holloway* court, the above-cited passage sounded in both tort and contract. The court determined that Paragraph 9 sufficiently alleged, per Rule 8 of the Indiana Rules of Trial Procedure, an offer, acceptance, and consideration.[361] Further, the court agreed that Paragraph 10 sufficiently alleged that Norpac breached its obligation to deliver unadulterated frozen food to Bob Evans.[362]

The court next examined, in turn, both Bob Evans's and Norpac's substantive claims that Holloway failed to set forth sufficient evidence to justify damages for

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356. 695 N.E.2d 991 (Ind. Ct. App. 1998).
357. *See id.* at 993.
358. *Id.* at 997.
359. *Id.* at 994.
360. *Id.*
361. *Id.*
362. *Id.*

breach of contract. Bob Evans argued "that the only damages placed at issue by Holloway were her emotional distress damages and that such damages are not recoverable for breach of contract."[363] The court agreed that emotional distress damages are not recoverable under a pure breach of contract theory, but that Holloway sought, in addition to recovery for emotional distress, recovery for her physical illness, multiple doctor visits, medications, and her absence from work.[364] Accordingly, the court reversed the trial court's grant of summary judgment, concluding that a genuine issue of material fact existed on whether Bob Evans's breach was a substantial factor that contributed to Holloway's aforementioned damages.[365]

Norpac made a similar argument, maintaining that Holloway failed to present sufficient evidence to support her breach of contract claim with respect to it. The court agreed, recognizing first that Holloway's breach of contract claim against Norpac was based on a third party beneficiary theory.[366] Holloway's claim failed because she did not designate any evidence regarding the terms of the contract between Norpac and Bob Evans, nor did she demonstrate that Norpac or Bob Evans intended that she receive a benefit by performance of the contract.[367] Thus, the court determined that the trial court did not err when it granted summary judgment to Norpac on the breach of contract issue.[368]

Finally, in *I.C.C. Protective Coatings, Inc. v. A.E. Staley Manufacturing Co.*,[369] the facts of which are discussed in detail earlier in this Article,[370] the appellate court affirmed a trial court's decision to allow Staley's "principal process engineer" to offer an opinion that the company "lost 2.6 million pounds of starch, at a cost of approximately $130,000, due to I.C.C.'s defective performance."[371] I.C.C. claimed that evidence of Staley's lost profits was irrelevant and speculative, and that the employee was incompetent to testify about lost profits.

According to the court, the Staley employee was familiar with the manufacturing process and that part of his job required him to estimate the

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363. *Id.* at 995.

364. *Id.* (citing Plummer v. Hollis, 11 N.E.2d 140 (Ind. 1937)).

365. *Id.*

366. *Id.* The court acknowledged that a third party beneficiary contract in Indiana exists when: (1) the parties intend to benefit the third party, (2) the contract imposes a duty on one of the parties in favor of the third party, and (3) the performance of the terms of the contract renders a direct benefit to the third party intended by the parties to the contract.

Id. at 995 (citing National Bd. of Examiners for Osteopathic Physicians and Surgeons, Inc. v. American Osteopathic Ass'n, 645 N.E.2d 608, 618 (Ind. Ct. App. 1994)).

367. *See Holloway*, 695 N.E.2d at 996.

368. *Id.*

369. 695 N.E.2d 1030 (Ind. Ct. App. 1998).

370. *See supra* Part I.A.1.

371. *I.C.C. Protective Coatings*, 695 N.E.2d at 1037.

revenue that would be created by a new project to determine whether the project was cost-effective.[372] The employee was also familiar with Staley's marketing and sales procedures. As such, the court was satisfied that he was competent to testify about lost profits and that his testimony provided a sufficient basis for the trial court's damage award.[373] The court also agreed that lost profit evidence was relevant because I.C.C.'s failure to comply with the specifications set forth in the agreement forced Staley to delay reactor operations until the work was corrected.[374]

H. Choice of Law

Indiana appellate courts resolved three cases during the survey period in which the parties raised choice of law issues in contract disputes, *Schaffert v. Jackson National Life Insurance Co.*,[375] *Cox v. Nichols*,[376] and *Hartford Accident & Indemnity Co. v. Dana Corp.*[377] All three cases involved construction of insurance policies and, as such, this limited Article will not treat the underlying facts or their substantive resolution in detail. They are, however, notable in the contract context because they each confirm Indiana's "most intimate contacts"[378] test for choice of law in contract cases involving interpretation of insurance policies. The "most intimate contacts" test focuses on five factors: (1) place of contracting; (2) place of negotiation; (3) place of performance; (4) location of subject matter of contract; (5) domicil, residence, nationality, place of incorporation and place of business of parties.[379]

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372. *Id.*

373. *Id.* In estimating lost profits, the engineer multiplied the number of pounds of starch that would have been produced during the delay by the net profit Staley earned per pound of starch. The court agreed that the evidence supported the damage award. *Id.*

374. *Id.*

375. 687 N.E.2d 230 (Ind. Ct. App. 1997).

376. 690 N.E.2d 750 (Ind. Ct. App. 1998).

377. 690 N.E.2d 285 (Ind. Ct. App. 1997).

378. The "most intimate contacts" test has been succinctly stated as follows: "'The court will consider all acts of the parties touching the transaction in relation to the several states involved and will apply the law of that state with which the facts are in most intimate contact.'" *Schaffert*, 687 N.E.2d at 233 (quoting Eby v. York-Div., Borg-Warner, 455 N.E.2d 623, 626 (Ind. Ct. App. 1983) (citation omitted)).

379. *See Hartford*, 690 N.E.2d at 291-94 (utilizing test to resolve whether to apply Ohio or Indiana law, ultimately determining that application of Indiana law was appropriate); *Schaffert*, 687 N.E.2d at 232-33 (applying factors to conclude that Illinois law applied rather than Indiana law); *see also* RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 188 (1971). Although it recognizes the "most intimate contacts" choice of law test when construing an insurance contract, the court's opinion in *Cox v. Nichols*, 690 N.E.2d 750 (Ind. Ct. App. 1998), never sets forth each of the test's factors in detail. Regardless, because the *Cox* court ultimately determined that it could not resolve the choice of law issue solely by looking to the contract itself, the *Cox* opinion also includes

II. SURVEY OF 1998 INDIANA BUSINESS LAW

A. Interest

1. Construction Contracts.—In *Indiana Erectors, Inc. v. Trustees of Indiana University*,[380] the facts of which are discussed in detail earlier in this Article,[381] Erectors appealed the trial court's award of prejudgment interest because the University had failed to comply with section 34-4-37-1 of the Indiana Code.[382] Citing the decision of *In re Johnson*,[383] the court noted that this statute provided for new substantive right to *tort* claimants, enabling such plaintiffs to recover prejudgment interest as a component of compensatory damages.[384] The court also noted that prejudgment interest had been permitted as a component of contract damages prior to the enactment of section 34-4-37-1 of the Indiana Code.[385] Given that the trial court awarded damages based on a breach of contract theory, the court held that the provisions of section 34-4-37-1 were inapplicable and affirmed the trial court's award of prejudgment interest.[386]

In *Hooker Builders, Inc. v. Smalley*,[387] Hooker Builders, Inc. ("Hooker") entered into an agreement with the Smalleys to construct their residence. After construction, a dispute arose regarding the amount owed by the Smalleys under the agreement.[388] The matter was submitted to an arbitrator, who determined that the Smalleys owed Hooker the cost of construction plus eight percent, resulting in an award of $82,571.92 for Hooker. Hooker filed a motion to reconsider, asking the arbitrator to include interest on the award.[389] The arbitrator denied Hooker's request and reaffirmed the arbitrator's award. Hooker then filed a motion to correct the arbitrator's award in Bartholomew County Superior Court No. 2. The trial court denied the motion and confirmed the award.[390] Thereafter, a subcontractor of Hooker's filed a mechanic's lien on the property. The Smalleys petitioned the court to order Hooker to accept the award of $82,571.92. The trial court granted the Smalleys request, ordering the Smalleys to pay the

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Indiana's three factor test utilized to determine choice of law in tort cases. *Cox*, 690 N.E.2d at 752 (citing Hubbard Mfg. Co., Inc. v. Greeson, 515 N.E.2d 1071, 1073 (Ind. 1987)).

380. 686 N.E.2d 878 (Ind. Ct. App. 1997)).

381. *See supra* Part I.D.6.

382. *Indiana Erectors*, 686 N.E.2d at 882.

383. 120 B.R. 461 (Bankr. N.D. Ind. 1990).

384. *Indiana Erectors*, 686 N.E.2d at 882.

385. *Id.* (citing Indianapolis Mach., Co. v. Cohen, 378 N.E.2d 931, 935 (1978)).

386. *Id.*

387. 691 N.E.2d 1256 (Ind. Ct. App. 1998).

388. *See id.* at 1257. The Smalleys contended the Hooker was due only the balance of the estimated contract price while Hooker contended the actual cost of construction controlled. *See id.*

389. *See id.*

390. *See id.*

award into the court, which award was eventually delivered to Hooker.[391]

Hooker appealed the trial court's denial of Hooker's motion to correct the arbitrator's award to include interest.[392] The court noted that an award of interest is available only if damages are readily ascertainable.[393] Because, Hooker failed to provide the court with a record of the trial court's proceedings, the court held that Hooker was not entitled to interest prior to the date of the arbitrator's award. However, because both parties agreed that the arbitrator's award was binding, the court awarded Hooker interest from the date of the award to the date of the trial court's judgment.[394]

2. Tender of Payment.—In *4-D Buildings., Inc. v. Palmore*,[395] 4-D Buildings, Inc. ("Builder") brought an action against The Golden Post, Inc. ("Kennel") requesting foreclosure of a mechanics lien for the construction of a building. Kennel counterclaimed against Builder claiming defective construction.[396] "Kennel admitted that it owed the amount secured by the mechanic's lien."[397] Builder agreed to accept a sum of $4,933.56 from Kennel in exchange for releasing Kennel from any further accumulation of prejudgment interest.[398] However, Kennel paid said amount, over Builder's objection, to the trial court. The trial court ruled that it would hold the payment pending resolution of the trial.[399] The trial court subsequently held that such payment to the court constituted proper tender by the Kennel to discontinue accumulation of prejudgment interest.[400] Builder appealed.

The *4-D Buildings* court noted that the award of prejudgment interest is based upon the idea that the plaintiff, during the course of litigation, is deprived of funds and is not made whole unless interest is included in the award.[401]

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391. *See id.*

392. As a threshold issue, the court rejected the Smalleys' claim that Hooker, by accepting the award and simultaneously executing a waiver for its receipt, waived the right to bring further claims. *Id.* The court's ruling was based on the facts that Hooker accepted the award at the Smalleys' request to remove the lien and was merely a credit against the ultimate judgment. *Id.*

393. *Id.* at 1258 (citing City of Indianapolis v. Twin Lakes Enters., Inc., 568 N.E.2d 1073, 1087 (Ind. Ct. App. 1991) (finding that damages are readily ascertainable where the trier of fact need not exercise its judgment to determine the amount of damages)).

394. *Id.* The court awarded further interest from the date of judgment to the date the Smalleys' paid the amount of the award to the trial court based on section 24-4.6-1-101 of the Indiana Code. *Id.*

395. 688 N.E.2d 918 (Ind. Ct. App. 1997).

396. *See id.* at 920.

397. *Id.*

398. *See id.*

399. *See id.*

400. *See id.*

401. *Id.* (citing Wayne Township v. Lutheran Hosp. of Ft. Wayne, Inc., 590 N.E.2d 1130, 1134 (Ind. Ct. App. 1992)).

However, a proper tender ends any further obligation to pay additional interest.[402] The court noted that a proper tender "generally requires full payment of the debt due, and *if refused*, the tender must be kept open by paying the full amount into court."[403] Because Kennel did not pay the tendered sum to Builder, Builder did not receive compensation for deprivation of sums due to Builder. Therefore, the court held that the tender was improper and did not serve to stem the accumulation of prejudgment interest.[404]

B. Banks and Banking

1. Fiduciary Relationship with Debtors.—In *The Huntington Mortgage Co. v. DeBrota*,[405] debtors on home mortgage loans originated by The Huntington Mortgage Company (the "Bank")[406] brought suit against the Bank for its collection private mortgage insurance ("PMI").[407] The Bank moved for summary judgment, which was denied by the trial court,[408] and then brought an interlocutory appeal. In its appeal, the Bank requested that the court grant its summary judgment motion against the debtors' claims for breach of contract, suppression of material facts, conversion, unjust enrichment, civil conspiracy, bailment and breach of fiduciary duty.[409]

In addressing the debtors' breach of contract claim, the court noted that the mortgage executed by the debtors contained sections requiring the payment of PMI premiums if payment of such conditions were a requirement for making the loan.[410] In determining whether PMI was a requirement for making the loan, the

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402. *See id.* (citing IND. CODE §§ 26-1-3.1-603(c), 34-2-24-1 (1998)).

403. *Id.* (emphasis in original) (citing IND. CODE § 34-2-24-1 (1998); Maddox v. Wright, 489 N.E.2d 133, 138 (Ind. Ct. App. 1996)).

404. *Id.* at 921. The court also addressed Builder's appeal of certain damages awarded Kennel on its counterclaims. Builder claimed that the trial court awarded Kennel damages for corrective actions that were for items beyond those contained in the agreement for construction between Builder and Kennel. *See id.* Thus, Builder argued, the trial court put Kennel into a better position than it would have been under the contract. While the court agreed with Builder's argument that an award for contractual damages is limited to the loss actually suffered, it noted that the additional items were necessitated to cure Builder's breach and therefore were permissible. *Id.* at 921-22.

405. 703 N.E.2d 160 (Ind. Ct. App. 1998).

406. The loans subsequently were sold by the Bank to Fannie Mae. *See id.* at 163.

407. *Id.* As the court notes, the secondary market requires debtors to pay PMI premiums when the loan to value ratio for the home mortgage loan is greater than eighty percent. *Id.* PMI protects the lender in the event that unpaid balance of a loan is greater than the value of the mortgaged property at foreclose. *See id.* at 163 n.3.

408. *Id.* at 163.

409. *Id.*

410. *Id.* at 164. The court cited the following provision:

> Funds for Taxes and Insurance. Subject to applicable law or to a written waiver

court reviewed the Bank's commitment letter, which specifically required such payments.[411] Moreover, the court pointed to the debtors' own testimony, wherein they admitted that they were aware that PMI would be required for their loan.[412] The court rejected the debtors' argument that the Bank was obligated contractually to enter into an agreement to discontinue PMI payments based on the plain meaning of the language in the mortgage permitting cessation of PMI payments when such requirement ends upon written agreement between a debtor and the Bank.[413] In addition to disagreeing regarding the "plain meaning" of the said language, the court further noted that the mortgage stated that PMI premiums are to be paid "until the Note is paid in full."[414] The debtor next argued that the Bank had the right to cancel PMI premiums given that the Fannie Mae servicing guidelines permit the Bank to cancel such premiums when the loan to value ratio of the loan reaches eighty percent.[415] The court, however, held that Fannie Mae's policy places discretion with the lender and confers no rights upon debtor.[416] Moreover, the court stated that the debtors' argument ignores the fact that lenders may desire PMI when the loan to value ratio is less than eighty percent for high risk borrowers, and that the Bank's policies included criteria for discontinuance of PMI insurance, such as reappraisal of the mortgaged property.[417] Therefore, the court held that the Bank had a contractual right to continue collection of PMI premiums from debtors.[418]

> by Lender, Borrower shall pay to Lender on the day monthly payments are due under the Note, until the Note is paid in full, a sum of ("Funds") for : . . . (e) yearly mortgage insurance premiums, if any; and (f) any sums payable by Borrower to Lender, in accordance with the provisions of paragraph 8, in lieu of the payments of mortgage insurance premiums.
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> * * *
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> Mortgage Insurance. If Lender required mortgage insurance as a condition of making the loan secured by this Security Instrument, Borrower shall pay the premiums required to maintain mortgage insurance in effect . . . until the requirement for mortgage insurance ends in accordance with any written agreement between Borrower and Lender or applicable law.

Id. at 164.

411. The commitment letter stated: "THIS COMMITMENT IS CONTINGENT UPON THE CONDITIONS AS NUMBERED BELOW: . . . (4) Receipt of mortgage insurance approval by coverage at 22%, AT TIME OF CLOSING." *Id.*

412. *Id.* at 165.

413. *Id.* at 164.

414. *See supra* note 409 and accompanying text.

415. *Huntington Mortgage*, 703 N.E.2d at 165.

416. *Id.* at 166 (citing Hinton v. Federal Nat'l Mortgage Ass'n, 945 F. Supp. 1052, 1056, 1059 (S.D. Tex. 1996)).

417. *Id.*

418. *Id.* In holding that the Bank had a right to collect the PMI premiums, the court found it unnecessary to address the debtors' claims for conversion and unjust enrichment. *Id.*

The court next considered whether the Bank had a fiduciary duty to debtors, such that the Bank was obligated to make certain disclosures to debtors.[419] The court first noted that, in Indiana, the general rule is that "'the mere existence of a relationship between parties of bank and customer or depositor does not create a special relationship of trust and confidence.'"[420] The court noted that, for a fiduciary relationship between bank and customer to be implied, special circumstances must exist wherein a weaker, less knowledgeable and/or dependant party puts confidence in the other, and that party wrongfully abuses the confidence.[421] The debtors asserted that the Bank's superior knowledge regarding PMI, control over the premiums and the purchase PMI, and its duties to provide an accounting for and properly escrow said funds gave rise to a fiduciary relationship. The court noted, however, that such circumstances exist in almost every relationship between a lender and a borrower.[422] The court cited the Eastern District of Louisiana's holding that although a lender, as an escrow agent for insurance premiums and taxes, does have certain fiduciary duties to safeguard and properly disburse funds, such duties do not encompass a duty secure the lowest premium rate, the best terms, or the best company any more than the escrow of tax payments imposes a duty to secure lower assessments.[423] Thus, the court held that the debtors had failed to establish special circumstances that would give rise to a fiduciary relationship.[424]

2. *Wrongful Dishonor.*—In *Wells v. Stone City Bank*,[425] Wells obtained a loan from the Stone City Bank (the "Bank") in the amount of $15,000 and opened a checking account with the Bank, into which the loan proceeds were

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419. *Id.* at 166-69. Specifically, the debtors alleged

> that [the Bank] had a duty to disclose the following: 1) that there was no written agreement or applicable law which required [the debtors] to pay PMI; 2) the true nature of the purpose and requirements for PMI; 3) the fact that [the debtors] could obtain PMI from the insurer of their choice; 4) the point at which [the debtors] were no longer required to pay PMI, if at all; 5) the criteria for discontinuing payment of PMI insurance premiums; . . . [and that] the premiums for PMI did not decrease as [the debtors] paid down the principal of the loan.

See id. at 166-67.

420. *Id.* at 167 (quoting Peoples Trust Bank v. Braun, 443 N.E.2d 875, 879 (Ind. Ct. App. 1983)).

421. *Id.*

422. *Id.*

423. *Id.* at 167-68 (citing Blair v. Source One Mortgage Servs. Corp., No. CIV.A. 96-2497, 1997 WL 250040, at *11 (E.D. La. May 9, 1997)).

424. *See id.* at 168. The court dispensed with the civil conspiracy claim because the debtors failed to raise any action of the Bank with regard to collection of PMI that was unlawful. *Id.* The bailment claim was dismissed by the court because it had held the Bank had a right to collect such PMI premiums and was not required to return said premiums to the debtors. *Id.* at 169. Therefore, no bailment had been created.

425. 691 N.E.2d 1246 (Ind. Ct. App. 1998).

deposited. Afterwards, Wells wrote three checks totaling $9,534.20, which the Bank did not honor.[426] Approximately three years later, Wells sued the Bank for wrongful dishonor, breach of contract, breach of the duty of good faith, and fraud, asking for $17.5 million in lost income, punitive damages, costs, and attorney fees.[427] The Bank moved for summary judgment, arguing that Wells' claims were barred by the two-year statute of limitations for personal injury claims.[428] Wells appealed, contending that his claims sounded in breach of contract, and therefore were subject to the six-year statute of limitations for contract claims.[429]

In determining which limitations period applied to Wells' claim, the court noted that if either of two statutes of limitation apply to a claim, any doubt as to which one to apply should be resolved in favor of applying the longer period.[430] Citing *Black's Law Dictionary*, the court noted that "a tort is a legal wrong to person or property, *independent of contract*."[431] However, the relationship between bank and depositor, particularly with regard to a checking account, is contractual in nature.[432] The court noted that Wells did not allege the breach of any duty in his claim against the Bank outside of the Bank's failure to comply with the terms of his contract for services.[433] The court rejected the Bank's argument that because some of Wells' claims, such as the claim for damage to reputation, are generally only available for libel, slander, abuse of process, malicious prosecution and interference with third party contract, that his claim was a tort action. The court noted that the reason damage to reputation was permitted in such claims is because such damages are a foreseeable results of such torts.[434] The court reasoned that a trial court, looking at the facts of this case, might determine that damage to reputation was a foreseeable result of the Bank's breach of its contract with Wells.[435] The court concluded that the possibility that a particular injury is not a foreseeable result of a particular breach of contract should not preclude a contract claim just because the consequential damage sought sounds more appropriately in tort.[436]

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426. *See id.* at 1248.

427. *See id.*

428. *See id.*; *see also* IND. CODE § 34-1-2-2 (1998).

429. *See Wells*, 691 N.E.2d at 1248; *see also* IND. CODE § 34-1-2-1 (1998).

430. *Wells*, 691 N.E.2d at 1249.

431. *Id.* (emphasis added by the court) (citing BLACK'S LAW DICTIONARY 1489 (6th ed. 1990)).

432. *Id.*

433. *Id.*

434. *Id.*

435. *Id.*

436. *Id.* at 1250. The court cited *Lawyers Title Insurance Corp. v. Pokraka*, 595 N.E.2d 244, 247 (Ind. 1992), for the proposition that recovery theories of fraud or breach of oral contract always involve injury to person or property and that applying the two-year statute of limitations to such claims would be tantamount to repealing the six-year statute of limitations for fraud and breach of

The court rejected Wells' claim of fraud in the Bank's misrepresentation that it would honor Wells' checks by opening an account and accepting his deposit.[437] The court observed that fraud requires a misrepresentation of a past or present fact.[438] However, the court noted that Wells' claims stated a cause of action for constructive fraud, which does not require a false statement of a past or present fact.[439] The elements of constructive fraud are: 1) a duty existing by virtue of the relationship between the parties; 2) representations or omissions made in violation of that duty; 3) reliance thereon by the complaining party; 4) injury to the complaining party as a proximate result thereof; and 5) the gaining of an advantage to the duty-bound party to this disadvantage of the complaining party.[440] The court held that the Bank's superior position with regard to its depositors, who depend on the bank to safeguard their funds and honor their checks, imposes a duty on a Bank sufficient for the first element of constructive fraud.[441] The court further held that Wells' allegations satisfied the remaining elements of constructive fraud.[442] Therefore, the court reversed the trial court's grant of summary judgment on the allegation of fraud.[443]

3. Failure to Abide by Loan Commitment.—In *Ohio Valley Plastics v. National City Bank*,[444] a loan officer for National City Bank (the "Bank") continued to assure the principal of Ohio Valley Plastics, Inc. (the "Borrower") that the Bank had approved Borrower's request for a line of credit, when, in fact, the loan request had never been submitted to the Bank's loan committee and had not been approved. Borrower then brought an action against the Bank for fraud and promissory estoppel alleging reliance damages including lost business opportunities, costs in delaying business plans, damage to reputation, stationary and other costs and increased interest costs due to a higher rate on the loan Borrower obtained with another lender.[445] The trial court granted the Bank's

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oral contract. *Wells*, 691 N.E.2d at 1249-50.

437. *Id.* at 1251.

438. *Id.* at 1250.

439. *Id.*

440. *Id.* at 1250-51 (citing Mullen v. Cogdell, 643 N.E.2d 390, 401 (Ind. Ct. App. 1994)).

441. *Id.* at 1251. The court declined to determine that the Bank's duty was a fiduciary one, but the court held that a fiduciary duty is not required for constructive fraud. *Id.*.

442. *Id.* The second criteria is satisfied by the allegation that the Bank breached its duty to honor Wells' checks, the third by the allegation that Wells relied on the Bank to honor his checks, the fourth by Wells allegation that he was injured, and the fifth by the allegation that the Bank gained interest income from the sham transaction. *See id.*

443. *Id.* In his dissent, Judge Rucker disagreed with the majority's holding that the cause of action sounded in contract. *Id.* (Rucker, J., dissenting). Focusing on the substance of the cause of action, rather than the manner in which it was pleaded, Judge Rucker noted that the claims for damage to reputation and credibility are for personal injuries, which are properly recoverable in a tort action. *Id.* at 1252.

444. 687 N.E.2d 260, 262 (Ind. Ct. App. 1997).

445. *See id.*

motion for summary judgement based on the Statute of Frauds.[446]

The Borrower appealed, arguing in the alternative that: (i) its claim did not rise out of a credit agreement but from the Bank's misrepresentations and therefore the Statute of Frauds does not apply or (ii) even if the Statute of Frauds does apply, equitable theories of constructive fraud and promissory estoppel remove the case from the Statute.[447] In addressing the Borrower's first contention, the court noted that "[t]he substance of an action, rather than its form, controls whether a particular statute" applies.[448] The court further noted the Indiana Supreme Court's admonition in *Ball v. Cox*[449] that courts closely adhere to the Statute of Frauds, less it be rendered impotent.[450] The court held that Indiana Code section 32-2-1.5-5, which applies to "an action upon *an agreement* with a creditor *to enter into* a new credit *agreement*,"[451] applies to all actions arising out of an agreement of a bank to loan money, whether they be characterized as breach of contract, fraud, deceit or promissory estoppel.[452]

In addressing the Borrower's second contention, the court noted that, based on *Whiteco Industries, Inc. v. Kopani*,[453] a claim of fraud or estoppel will not remove a case from the Statute of Frauds.[454] To so rule, the court continued, would render the statute meaningless as every plaintiff would assert an oral promise estopped the statute's requirement of a writing.[455] In order for promissory estoppel to remove a case from the Statute of Frauds, the plaintiff must demonstrate the "'infliction of an unjust and unconscionable injury.'"[456] In the case at bar, the court held that Borrower's reliance damages did not rise to that level.[457] The court went on dismiss the Borrower's claim for constructive fraud because the Borrower's allegations did not satisfy the requirement that the Bank gain from its alleged fraud.[458] Lastly, the court distinguished the case of

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446. *See id.* Indiana's Statute of Frauds, IND. CODE § 32-2-1.5-5 (1998), provides in part: "A debtor may bring an action upon an agreement with a creditor to enter into a new credit agreement . . . only if the agreement: (1) is in writing; (2) sets forth all the material terms and conditions of the agreement; and (3) is signed by the creditor and debtor."

447. *Ohio Valley Plastics*, 687 N.E.2d at 263.

448. *Id.* (citing Shideler v. Dwyer, 417 N.E.2d 281, 285-86 (Ind. 1981); INB Nat'l Bank v. Moran Elec. Serv., Inc., 608 N.E.2d 702, 706 (Ind. Ct. App. 1993)).

449. 7 Ind. 453 (1856).

450. *Ohio Valley Plastics*, 687 N.E.2d at 263.

451. IND. CODE § 32-2-1-1.5-5 (1998) (emphasis added).

452. *Ohio Valley Plastics*, 687 N.E.2d at 263-64.

453. 514 N.E.2d 840 (Ind. Ct. App. 1987).

454. *Ohio Valley Plastics*, 687 N.E.2d at 264.

455. *Id.* (citing *Whiteco Indus.*, 514 N.E.2d at 844).

456. *Id.* (quoting *Whiteco Indus.*, 514 N.E.2d at 845).

457. *Id.*

458. *Id. See supra* note 418 and accompanying text (discussing the elements of constructive fraud).

First National Bank v. Logan Manufacturing Co.,[459] wherein the Indiana Supreme Court did permit a borrower to collect reliance damages for breach of an oral agreement to loan money, because that case was decided prior to the effective date of the statute in question.[460]

4. Conversion of Negotiable Instruments Fraudulently Endorsed by Fiduciary.—In *UNR-Rohn, Inc. v. Summit Bank of Clinton County*,[461] the court of appeals addressed whether a bank could be held liable when it cashed hundreds of checks for an authorized signor on a corporate account, which funds later were determined to be embezzled.[462] An employee of UNR-Rohn, Inc. ("Depositor") had authorized a certain employee to endorse checks payable to Depositor. In 1984, the employee began to cash third-party checks at NBD Bank (the "Bank") payable to Depositor and continued this practice until 1991, by which time the employee had embezzled approximately $182,000.[463] Depositor brought an action against the Bank under Indiana Code section 26-1-3-419[464] for breach of an alleged duty to deposit said checks to Depositor's account rather than cash them. The Bank moved for summary judgment based on the Uniform Fiduciary Act ("UFA")[465] and the statute of limitations. The trial court granted the Bank's motion with regard to the UFA but denied its motion with regard to the statute of limitations defense.[466] Both parties appealed.

The court first reviewed Indiana Code sections 30-2-4-4 and 30-2-4-9 and determined that, if a fiduciary is empowered to endorse checks, the UFA protects a bank cashing a check endorsed by such fiduciary unless the bank has (i) actual knowledge that the fiduciary is breaching its duty or (ii) knowledge of sufficient facts that the bank's action in dealing with such fiduciary is in bad faith.[467] Although the UFA does not define "bad faith," the court noted that other courts addressing whether a bank acted with bad faith under the UFA have examined "'whether it was "commercially" unjustifiable for the payee to disregard and refuse to learn facts readily available.'"[468] Because the Bank was the moving party, the Bank had the burden of establishing that no genuine issue of material fact existed with regard to whether it acted in bad faith. The court noted that the Bank permitted the employee of Depositor to deposit several hundred corporate checks into his personal account, yet "merely relied upon general assertions in

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459. 577 N.E.2d 949 (Ind. 1991).

460. *Ohio Valley Plastics*, 687 N.E.2d at 265.

461. 687 N.E.2d 235 (Ind. Ct. App. 1997).

462. *Id.* at 236-37.

463. *See id.*

464. IND. CODE § 26-1-3-419 (repealed by P.L. 222-1993, § 58, effective July 1, 1994) (recodified as amended at IND. CODE § 26-1-3.1-420 (1998)).

465. IND. CODE §§ 30-2-4-1 to -14 (1998).

466. *UNR-Rohn*, 687 N.E.2d at 237.

467. *Id.* at 238-39 (citing IND. CODE §§ 30-2-4-4, -9 (1998)).

468. *Id.* at 239 (quoting Appley v. West, 832 F.2d 1021, 1031 (7th Cir. 1987) (stating that "[a]t some point, obvious circumstances become so cogent that it is 'bad faith' to remain passive").

its pleadings that it acted in good faith and that it lacked any knowledge of any breach of [the employee's] fiduciary duty.'"[469] The court then held that the Bank did not meet its burden of establishing that no genuine issue of material fact existed by merely asserting good faith, and reversed the trial court's grant of summary judgement on this issue.[470]

In addressing the Bank's cross appeal for denial of summary judgment, the court focused on determining the point in time at which the Depositor's cause of action accrued under Indiana Code section 34-1-2-2[471] for the purpose of determining whether the statute of limitations had lapsed.[472] The court first noted that Indiana courts, in determining when a cause of action accrues under Indiana Code section 34-1-2-2, consistently have applied the discovery rule whereby a cause action begins accruing at the time the plaintiff knew, or with the exercise of ordinary diligence, could have discovered that a cause of action against another has arisen.[473] The court concluded that in Indiana, the discovery rule applies to the accrual of any tort action.[474] The Bank argued that no Indiana court had applied the discovery rule to a cause of action involving the conversion of negotiable instruments and cited a litany of cases from other jurisdictions that declined to apply the discovery rule to Indiana Code section 26-1-3-419.[475] The court, however, reasoned that it would be inconsistent with Indiana's system of jurisprudence to carve out an exception to the discovery rule for tort actions involving conversion of negotiable instruments.[476] Therefore, the court remanded the case to the trial court to apply the discovery rule to the Depositor's cause of action under Indiana Code section 26-1-3-419 and to determine whether the Depositor's claims were time barred.[477]

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469. *Id.* at 239.

470. *Id.*

471. IND. CODE § 34-1-2-2 (1998).

472. *UNR-Rohn*, 687 N.E.2d at 239. The court also noted that both parties agreed that the two year statute of limitations set forth in Indiana Code section 34-1-2-2(1) (1998) applied to the Depositor's claims. *Id.* at 240.

473. *Id.* at 240 (noting that the discovery rule "'is based on the reasoning that it is inconsistent with our system of jurisprudence to require a claimant to bring [a] cause of action'" before the plaintiff could know, with due diligence, that such cause of action existed).

474. *Id.* (citing Wehling v. Citizens Nat'l Bank, 586 N.E.2d 840, 842-43 (Ind. 1992); Habig v. Bruning, 613 N.E.2d 61, 64 (Ind. Ct. App. 1993)).

475. The court may have actually meant to refer to U.C.C. 3-419 based upon the court's reference to this statute in footnote 5. *Id.* at 241 & n.5.

476. *Id.* at 241. The court did recognize in a footnote that other jurisdictions had declined to apply the discovery rule to causes of action under U.C.C. 3-419 in the absence of fraudulent concealment based on "U.C.C. policies of finality, negotiability and uniformity." *Id.* at 241 n.5.

477. *Id.* at 241.

C. Associations

1. Barring Claims by Members Against Associations.—In *Biereichel v. Smith*,[478] the court of appeals held that a member of an unincorporated association could not sue the association for the tortious acts of another member. In *Biereichel*, the plaintiff, a member of a union, went to the union's "office to obtain information regarding work opportunities."[479] After a discussion with a union member employed by the union as its business manager/representative, the plaintiff was attacked by the union business manager and was severely injured.[480] The plaintiff filed an action against the union and the union was granted partial summary judgment by the trial court based "on the general rule in Indiana that members of an unincorporated association cannot sue the association for the tortious acts of one or more of its members."[481]

On appeal, the plaintiff contended that the court of appeal's recent ruling in *Hanson v. St. Luke's United Methodist*[482] required the court to reverse the summary judgment ruling.[483] In *Hanson*, the court of appeals carved out an exception to the general rule and refused to dismiss a lawsuit brought by a member against her church for injuries she sustained during a fall in the church's parking lot.[484] However, because the Indiana Supreme Court had granted transfer in *Hanson*, that decision did not constitute binding precedent.[485] The *Biereichel* court then reviewed the supreme court's decision in *Calvary Baptist Church v. Joseph*,[486] which articulated the general rule that "members of an unincorporated association cannot sue the association for the tortious acts of one or more of its members."[487] In *Calvary*, the supreme court noted that other jurisdictions had created an exception to this general rule for highly organized and centralized associations and cited the California Supreme Court's decision in *Marshall v.*

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478. 693 N.E.2d 634, 638 (Ind. Ct. App. 1998).
479. *Id.* at 635.
480. *See id.*
481. *Id.* at 636
482. 682 N.E.2d 1314 (Ind. Ct. App. 1997).
483. *Biereichel*, 693 N.E.2d at 636.
484. *Id.*
485. *See id.*
486. 522 N.E.2d 371 (Ind. 1988).
487. *Biereichel*, 693 N.E.2d at 636. The court quoted from *Calvary* the theory behind the general rule:

> [T]he members of an unincorporated association are engaged in a joint enterprise. The negligence of each member in the prosecution of that enterprise is imputable to each and every other member so that the member who has suffered damages through the tortious conduct of another member of the association may not recover from the association for such damage. It would be akin to the person suing himself as each member becomes both a principal and an agent as to all other members for the actions of the group itself.

Id. (quoting *Calvary Baptist Church*, 522 N.E.2d at 374-75).

International Longshoremans' and Warehousemans' Union.[488] The *Biereichel* court noted that, although the Supreme Court in *Calvary* did recognize the wisdom of this exception, the *Calvary* court declined to adopt it.[489] The *Biereichel* court likewise declined to adopt the exception, as it believed that any abrogation of a general rule of law would be best left to the Indiana Supreme Court.[490]

The plaintiff then argued that the general rule in Indiana should not be applied when the member committing the tortious conduct was not engaged in an association activity or joint enterprise.[491] The *Biereichel* court rejected this argument finding that the *Calvary* court did not set out any such requirement for application of the general rule.[492] Finally, the plaintiff argued that summary judgement was inappropriate because the association manager's acts arguably were intentional and therefore the general rule set forth in *Calvary* does not apply.[493] The *Biereichel* court declined to address this argument because the plaintiff failed to support this contention with an argument or relevant authority.[494] Therefore, the *Biereichel* court affirmed the trial court's grant of summary judgment in favor of the defendant union.[495]

In *Menard Inc. v. Dage-MTI, Inc.*,[496] the court of appeals addressed whether the president of a corporation could bind the corporation when he did not have express authority to sell the corporation's property. Dage-MTI, Inc. ("Dage") is a closely held Indiana corporation whose president was Arthur Sterling ("Sterling").[497] Menard, Inc. ("Menard") forwarded a formal offer to Sterling for the purchase of certain real estate owned by Dage. Sterling circulated the offer to the Dage directors who had a disfavorable opinion of the sale.[498] Thus, Sterling let the offer lapse. Later, Sterling informed Menard's agent that the Dage board of directors had objected to various provisions contained in the offer.[499]

Subsequently, Menard indicated that it would make a second offer for a

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488. 371 P.2d 987 (1962) (recognizing an exception for large international labor unions satisfying the following "two-part test: (i) whether the association possesses a separate legal existence from its members, and (ii) whether the members retain direct control over the operations of the association").

489. *Biereichel*, 693 N.E.2d at 637.

490. *Id.*

491. *See id.*

492. *Id.* at 637.

493. *Id.* at 637-38.

494. *Id.* at 638.

495. *Id.*

496. 698 N.E.2d 1227, 1229 (Ind. Ct. App. 1998).

497. *See id.*

498. *See id.*

499. *See id.*

larger portion of the real estate.[500] Sterling drafted a resolution that authorized Sterling to "offer and sell" the real estate. Sterling was told by the board of directors to revise the resolution to read "offer for sale."[501] Sterling was further informed by the board that he could only offer the real estate to Menard at a particular price and could not negotiate the terms of a sale without board acceptance.[502] When Menard forwarded a second proposal to purchase the real estate, the agreement contained the same objectionable provisions found in the first proposal. Nevertheless, Sterling negotiated several minor changes to the agreement and then signed the revised offer on behalf of Dage without approval of the board of directors.[503] The offer included a provision stating that Sterling was duly authorized to sign the agreement and to bind Dage.[504] Once the board of directors became aware of the Menard agreement, the board ordered Sterling to "extricate Dade from the agreement" and retained counsel to put Menard on notice that the board questioned and intended to contest the agreement's enforceability.[505] Menard ultimately filed suit for specific performance against Dage. The trial court ruled in favor of Dage and Menard appealed.

On appeal, Menard first argued that the trial court erred concluding that Sterling lacked express authority to sign the agreement.[506] The *Menard* court stated a fundamental tenet of agency law that "'an agent has no authority to act contrary to the known wishes and instructions of his principal.'"[507] Moreover, "'an agent is authorized to do [only] what is reasonable for him to infer that the principal desires him to do in light of the principal's manifestations and the facts as he knows . . . them or should know them at the time.'"[508] The *Menard* court noted that the resolution drafted by Sterling was specifically altered to change the language to "offer for sale." Further, the Dage board of directors "informed Sterling that any offer made by Menard would require board review and acceptance."[509] Thus, the *Menard* court concurred with the trial court's ruling that Sterling lacked express authority to bind Dage to the terms of Menard's agreement.[510] Menard cited *Blairex Laboratories, Inc. v. Clobes*,[511] wherein the court of appeals held that an agent had express authority from its principal despite the fact that one member of the board of directors indicated that he would

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500. *Id.*

501. *Id.* at 1229-30.

502. *See id.* at 1230.

503. *See id.*

504. *See id.*

505. *Id.*

506. *See id.*

507. *Id.* (quoting Old Security Life Ins. Co. v. Continental Ill. Nat'l Bank & Trust Co., 740 F.2d 1384, 1391 (7th Cir. 1984)).

508. *Id.* at 1230-31 (quoting RESTATEMENT (SECOND) OF AGENCY § 33 & cmt. a (1957)).

509. *Id.* at 1231.

510. *Id.*

511. 599 N.E.2d 233 (Ind. Ct. App. 1992).

like to see the agent enter into a contract with certain provisions which the contract ultimately did not contain.[512] The *Menard* court distinguished *Blairex* because the Dage board of directors' expressions were not merely a desire to see certain terms in the agreement, but rather specific directives that Sterling's authority was limited only to solicitation of offers.[513]

Menard also argued that the trial court erred in finding that Sterling did not have apparent authority to enter into a binding agreement.[514] "Apparent authority refers to a third party's reasonable belief that the principal has authorized the acts of its agent."[515] Apparent authority "arises from the principal's indirect or direct manifestations to a third party, and it cannot arise from the representations or acts of the agent."[516] Menard relied on *Pollas v. Hardware Wholesalers, Inc.*,[517] and related cases for the proposition that the use of Sterling as a sole negotiator was an indirect manifestation of Sterling's apparent authority. Although a communication of authority made solely by an agent normally will not result in apparent authority, the *Pollas* court held that when a principal "'places an agent in the position of sole negotiator on [its] behalf, it may be reasonable for a third person to believe that the agent possesses authority to act for the principal.'"[518] However, in *Menard*, "the trial court concluded that, because Sterling had informed Menard of his need for board approval before entering into the agreement . . . , Menard could not have reasonably believed that Sterling possessed authority to bind Dage to the agreement."[519] Menard further argued that *Pollas* and related cases require a finding that an agent has apparent authority when the principal appoints that agent as a sole negotiator.[520] The *Menard* court dismissed this argument, stating that *Pollas* and its progeny permit a finding of apparent authority but do not *require* such a finding.[521]

2. Court's Reluctance to Interfere with Internal Affairs of Voluntary Associations.—In *Indiana High School Athletic Ass'n v. Reyes*,[522] the Indiana Supreme Court declined to interpret and enforce the rules of the Indiana High School Athletic Association ("IHSAA") leaving the interpretation of IHSAA rules to its members. In *Reyes*, a student baseball player was prohibited from playing high school baseball by the IHSAA because that student, who had been

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512. *Menard*, 698 N.E.2d at 1231.

513. *Id.*

514. *See id.*

515. *Id.* (citing Pepkowski v. Life of Ind. Ins. Co., 535 N.E.2d 1164, 1166-67 (Ind. Ct. App. 1989)).

516. *Id.* (citing Drake v. Maid-Rite Co., 681 N.E.2d 734, 737-38 (Ind. Ct. App. 1997), *reh'g denied*; *Pepkowski*, 535 N.E.2d at 1166-67).

517. 663 N.E.2d 1188 (Ind. Ct. App. 1996), *reh'g denied.*

518. *Menard*, 698 N.E.2d at 1232 (quoting *Pollas*, 663 N.E.2d at 67).

519. *Id.*

520. *See id.*

521. *Id.*

522. 694 N.E.2d 249, 257 (Ind. 1997).

held back one year in school in Puerto Rico before moving to Indiana, would play more seasons of high school sports than permitted by IHSAA eligibility rules.[523] The IHSAA's Eight Semester Rule places a maximum on the number of semesters that a student athlete may play high school sports.[524] The student petitioned the IHSAA for an additional year of eligibility under the IHSAA Hardship Rule and was denied.[525] The student filed suit for injunctive relief, arguing that the IHSAA Executive Committee's decision in his case was arbitrary and capricious and violated his right to equal privileges and immunities under Article 1, Section 23, of the Indiana Constitution.[526] The trial court issued a temporary restraining order preventing the IHSAA and the high school from enforcing the Eight Semester Rule against the student.[527] The trial court subsequently rejected the findings of the IHSAA's decision with regard to the student's eligibility and issued a permanent injunction against the IHSAA and the high school from enforcing the Eight Semester Rule against the student.[528] The trial court also prohibited the IHSAA from sanctioning the high school under its Restitution Rule for the school's compliance with the court order.[529] The IHSAA initiated an appeal and filed a petition to stay the judgment pending appeal with the trial court.[530] The trial court denied the petition to stay.[531] The court of appeals reversed the trial court's ruling

> and held that (i) the IHSAA's determination to deny [the student's] application for an exception under the hardship rule was not arbitrary and capricious; (ii) the IHSAA's decision to deny [the student's] request for another year of eligibility was state action subject to review under Article 1, Section 23 of the Indiana Constitution; (iii) the Eight Semester Rule and the hardship rule did not violate the [student's] right to equal

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523. *Id.* at 252-53.

524. *Id.* at 253.

525. *Id.* The IHSAA hardship rule provides:

> The Commissioner or his designee or the Committee shall have the authority to set aside the effect any Rule when, in the opinion of the Commissioner or his designee or the Committee:
>
> a. Strict enforcement of the Rule in the particular case will not serve to accomplish the purpose of the Rule;
>
> b. The spirit of the Rule has not been violated; and
>
> c. There exists in the particular case circumstances showing undue hardship which would result from enforcement of the Rule.

Id. at 253 n.2.

526. *Id.* at 253.

527. *See id.*

528. *See id.*

529. *Id.*

530. *Id.*

531. *Id.*

> privileges and immunities under Article I, Section 23 of the Indiana Constitution; and (iv) the IHSAA Restitution Rule is valid.[532]

The high school then appealed the IHSAA's application of the Restitution Rule to it, which required the school to forfeit victories, return trophies and awards and return certain funding in the event that an ineligible student athlete participated in violation of the IHSAA eligibility rules, even if such participation was in accordance with an injunction or restraining order that is later vacated.[533]

On appeal, the high school did not challenge the first three parts of the court of appeal's decision, but did challenge the validity of the Restitution Rule.[534] The high school apparently relied upon the court of appeals case, *Indiana High School Athletic Ass'n v. Avant*,[535] for the proposition that the IHSAA Restitution Rule violates the public policy of Indiana by penalizing schools and students for complying with court orders.[536] The *Avant* court analogized the application of the Restitution Rule to a situation where a court finds a statute to be unconstitutional, noting that because of "'the de facto existence and reliance upon [the statute's] validity, [the statute] has practical consequences which cannot be justly ignored.'"[537] The *Reyes* court found fault in the *Avant* court's analogy, which was based on the reasoning in *Martin v. Ben Davis Conservancy*

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532. *Id.*

533. *Id.* at 254. The Restitution Rule provides:

> If a student is ineligible according to [IHSAA] Rules but is permitted to participate in interschool competition contrary to [IHSAA] Rules but in accordance with the terms of a court restraining order or injunction against the student's school and/or the [IHSAA] and injunction is subsequently voluntarily vacated, stayed, reversed or it is finally determined by the courts that injunctive relief is not or was not justified, any one or more of the following action(s) against such school in the interest of restitution and fairness to competing schools shall be taken:
>
> a. Require individual or team records and performances achieved during participation by such ineligible student to be vacated or stricken;
>
> b. Require team victories to be forfeited to opponents;
>
> c. Require team or individual awards earned be returned to the association; and/or
>
> d. If the school has received or would receive any funds from an [IHSAA] tournament series in which the ineligible individual has participated, require the school to forfeit its share of net receipts from such competition, and if said receipts have not been distributed, authorize the withholding of such receipts by the [IHSAA].

Id. at 254 n.3.

534. *Id.* at 253-54. The high school contended that a split in authority existed between decisions by two courts of appeal and asked that the supreme court resolve the dispute. *See id.*

535. 650 N.E.2d 1164 (Ind. Ct. App. 1995).

536. *See Reyes*, 694 N.E.2d at 254-55.

537. *Id.* at 255 (quoting *Avant*, 650 N.E.2d at 1171 (quoting United REMC v. Indiana Mich. Power Co., 648 N.E.2d 1194 (Ind. Ct. App. 1995))).

District.[538] In *Martin*, the Indiana Supreme Court held that although an action generally is not sustainable if based upon an unconstitutional statute, a final judgment that is based upon the unconstitutional statute but rendered prior to the declaration of unconstitutionality is sustainable.[539] The *Avant* court concluded that the rationale of *Martin* renders the Restitution Rule unreasonable in that it penalizes persons relying on a trial court's ruling.[540] The *Reyes* court disagreed with the *Avant* court's reasoning, stating that the *Martin* exception does not apply because the trial court's injunction in *Reyes* was not a final judgment.[541]

The high school next argued that, despite the general Indiana rule that courts exercise limited interference with the internal affairs and rules of a voluntary membership associations, courts historically have applied heightened scrutiny to IHSAA decisions.[542] The *Reyes* court noted that there are some exceptions to this general rule.[543] For example, in *State ex Rel. Givens*,[544] the supreme court carved out an exception where the decision of the voluntary membership association infringed upon a member's liberty or property rights.[545] Another exception noted by the *Reyes* court is where the association's decision constitutes fraud or other illegality.[546] The *Reyes* court noted that certain courts of appeal decisions suggested a further exception where the association applies its rules in an arbitrary, discriminatory or malicious manner or the association rules require due process.[547] The *Reyes* court rejected any additional exceptions to the general rule stating that "[a]bsent fraud, other illegality, or abuse of civil or property rights having their origin elsewhere in law, Indiana courts will not interfere in the internal affairs of voluntary membership associations."[548] The *Reyes* court distinguished cases applying an arbitrary and capricious standard to the actions of the IHSAA based on the fact that those cases involved a student athlete's challenge to an IHSAA decision rather than a school's challenge to an IHSAA rule.[549] Although the *Reyes* court held that Indiana courts will continue to apply an arbitrary and capricious standard to IHSAA decisions affecting students, it will not apply such standard to the IHSAA's decisions regarding member schools.[550]

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538. 153 N.E.2d 125 (1958).
539. *Reyes*, 694 N.E.2d at 255.
540. *Id.* (quoting *Avant*, 650 N.E.2d at 1171).
541. *Id.*
542. *See id.*
543. *Id.* at 256.
544. 117 N.E.2d 553 (1954).
545. *Reyes*, 694 N.E.2d at 256.
546. *Id.* (citing Randolph v. Leeman, 146 N.E.2d 267, 272 (Ind. App. 1957)).
547. *Id.* (citing United States Auto Club v. Woodward, 460 N.E.2d 1255, 1261 (Ind. Ct. App. 1984); Terrell v. Palomino Horse Breeders of Am., 414 N.E.2d 332, 335 (Ind. Ct. App. 1980)).
548. *Id.*
549. *Id.* at 257.
550. *Id.*

Finally, the high school argued that the Restitution Rule was inherently contemptuous of the judiciary[551] by punishing schools for following a court's orders. However, the *Reyes* court likened voluntary membership and membership association rules to contracts. First, the court noted a variety of circumstances where contracts will allocate risks of unfavorable litigation results between parties.[552] For example, the *Reyes* court noted that "[c]ouples may sign prenuptial agreements dictating what is to occur should a trial judge determine that the prenuptial agreement is unenforceable."[553] The court concluded that such agreements show no disrespect for the courts, and neither did the Restitution Rule that constitutes an agreement between the IHSAA members allocating the risks of litigating IHSAA rules and balancing competing member interests.[554]

D. Limited Liability Companies: Allocation for Tax Purposes Requiring Cash Distributions

In *Five Star Concrete, L.L.C. v. Klink, Inc.*,[555] the court of appeals addressed whether a dissociated member of a limited liability company had a right to receive a cash distribution equal to the net income allocated to such member for tax purposes. A company ("Klink") formed a limited liability company called Five Star Concrete, L.L.C. (the "Five Star") with four other corporations, all engaged in supplying ready mix concrete, "in order to furnish concrete to large construction projects."[556] After a period of time, Klink disassociated from Five Star and, pursuant to the operating agreement for Five Star, received a payment from it for the market value of the limited liability company's units.[557] At Five Star's fiscal year end, it allocated $31,889 in profits to Klink for tax purposes.[558] Klink subsequently sued Five Star for a distribution of cash equal to the profits allocated to Klink for tax purposes.[559] The trial court granted Klink's motion for summary judgment and denied Five Star's cross motion for summary judgment.[560] Five Star appealed the trial court's grant of summary judgment on the issue of whether Klink, as a dissociated member of Five Star, had a legal right to receive a cash distribution equal to the net income allocated to Klink for tax purposes.[561] In appealing the denial of its cross motion for summary judgment, Five Star raised two additional issues: (i) whether Klink affirmatively divested itself of all economic interests in Five Star when it sold its membership units to

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551. *Id.*
552. *Id.*
553. *Id.*
554. *Id.* at 257-58.
555. 693 N.E.2d 583, 584 (Ind. Ct. App. 1998).
556. *Id.* at 585.
557. *See id.* at 585, 587.
558. *See id.* at 585.
559. *See id.*
560. *See id.*
561. *See id.* at 586.

Five Star and (ii) whether the method of valuing Klink's economic interest demonstrates that Klink was paid the current fair market value of its entire interest in Five Star[562]

First, the *Five Star* court addressed whether Klink had a legal right to receive a cash distribution based on the facts stated above.[563] The *Five Star* court noted that no provision in the Indiana Business Flexibility Act (the "Act")[564] "creates an automatic legal right to receive a distribution in the amount of [allocated] income, even when a member is withdrawing from the [limited liability company]."[565] The court further noted that such distributions, in some instances, would be unlawful.[566] In particular, the court noted that a distribution may be unlawful when it would cause a limited liability company to become insolvent.[567] The court further noted that Five Star's operating agreement was silent regarding the timing and amount of distributions and that, under the Act, such decisions are made by a majority of the members.[568] Finally, the *Five Star* court noted that limited liability companies, like partnerships, are pass-through entities receiving conduit treatment under income tax law, meaning "that allocations occur regardless of the magnitude or timing of distributions."[569] Therefore, the *Five Star* court held that Klink was not entitled, as a disassociated member of a limited liability company, to a cash distribution equal to its allocations of profits for the year.[570]

The *Five Star* court next addressed Five Star's argument that, because Klink sold its membership units, it divested itself of any economic interest in any

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562. *See id.* at 587.

563. *Id.* at 586.

564. IND. CODE §§ 23-18-1-1 to -13-1 (1998).

565. *Five Star Concrete*, 693 N.E.2d at 586.

566. *Id.* (citing IND. CODE § 23-18-5-6 (1998); United States v. Basye, 410 U.S. 441, 453 (1973)).

567. *Id.* at 586 n.4. The court specifically identifies Indiana Code section 23-185-6 (1998), which states that

> A distribution may not be made if after giving effect to the distribution:
>
> (1) [t]he limited liability company would not be able to pay its debts as the debts become due in the usual course of business; or (2) the limited liability company's total assets would be less than the sum of its total liabilities plus, unless the operating agreement permits otherwise, the amount that would be needed if the affairs of the limited liability company were to be wound up at the time of the distribution to satisfy any preferential rights that are superior to the rights of members receiving the distribution.

IND. CODE § 23-185-6 (1998).

568. *Five Star Concrete*, 693 N.E.2d at 586. The court noted that Five Star had made an earlier distribution to its members in which Klink received $12,500. *Id.*

569. *Id.* (citing BLACK'S LAW DICTIONARY 75 (6th ed. 1990)).

570. *Id.*

distributions of the limited liability company.[571] In examining the operating agreement for Five Star, the *Five Star* court observed that a "unit" is defined as "'an interest in the Company representing a contribution to capital.'"[572] The *Five Star* court observed that this definition of the term "unit" supported Klink's argument that it sold less than all of its economic rights in Five Star when it sold its membership units.[573] However, the *Five Star* court observed that under the same operating agreement, "each unit generally entitled the members to one vote and to a proportionate share of the [limited liability company's] net income, gains, losses, deductions and credits."[574] The *Five Star* court concluded that parties could reasonably differ as to the meaning of the word "unit" under the operating agreement and whether the sale of a unit constituted a transfer of all rights to future distributions of Klink.[575] Thus, the *Five Star* court held that the trial court properly denied Five Star's motion for summary judgment.[576]

Finally, the court addressed whether the trial court properly denied Five Star's motion for summary judgment based on its argument that, based on the fair market value of Klink's interest in Five Star, Five Star's purchase price for Klink's units included all potential distributions from Five Star.[577] The *Five Star* court noted that the "[v]aluing of an interest of a member is a 'complex task,' more of a business matter than a legal one."[578] Thus, the *Five Star* court concluded that a determination of market value is an issue of fact and not appropriate for summary judgment.[579]

E. Corporations

1. Dissenter's Right Statute as Exclusive Remedy.—In *Settles v. Leslie*,[580] The Indiana Court of Appeals discussed "whether the Indiana Dissenters Right statute[581] [("IDR")] provides the exclusive remedy for minority shareholders of a closely held corporation claiming breach of fiduciary duty by the corporation's majority shareholders."[582] In *Settles*, the majority shareholders (the "Majority Shareholders") of Mi-Tech Metals, Incorporated ("Mi-Tech") decided to sell the

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571. *Id.* at 587.
572. *Id.* (quoting Five Star Concrete, Inc. Operating Agreement).
573. *Id.*
574. *Id.*
575. *Id.*
576. *Id.*
577. *Id.*
578. *Id.* (citing PAUL J. GALANTI, 17 INDIANA PRACTICE, BUSINESS ORGANIZATIONS § 6.7 (1991)).
579. *Id.*
580. 701 N.E.2d 849 (Ind. Ct. App. 1998).
581. IND. CODE §§ 23-1-44-1 to -20 (1998).
582. *Settles*, 701 N.E.2d at 850.

company after the death of a key employee.[583] Mi-Tech successfully negotiated the merger of Mi-Tech with another company, which merger was objected to by minority shareholders (the "Minority Shareholders").[584] A special meeting of the shareholders of Mi-Tech was scheduled for September 12, 1994 to consider the proposed merger.[585] Just three days prior to the special meeting on September 9, 1994, the Minority Shareholders filed a complaint for a temporary restraining order to enjoin Mi-Tech's directors from voting on the proposed merger.[586] In their complaint, the Minority Shareholders alleged that the Majority Shareholders misappropriated Mi-Tech's funds by "(1) overcompensating themselves, (2) failing to pay dividends, and (3) receiving excessive compensation for employment contracts and non-competition agreements in connection with a corporate merger." The court denied the Minority Shareholders' request for the temporary restraining order.[587] At the special shareholders meeting, the Minority Shareholders, represented by counsel, delivered a Notice of Dissent regarding the merger stating that:

> Notice is hereby given that [the Minority Shareholders] . . . express and state their dissent with the proposed Plan of Merger of Mi-Tech Metals, Inc. with Birco, Inc.:
> 1. That [the Minority Shareholders] are shareholders entitled to vote on the proposed merger.
> 2. That it is the intent of [the Minority Shareholders] to demand payment for their shareholder's shares if the proposed action is effectuated.
> 3. That [the Minority Shareholders] further intend to retain all other rights of a shareholder, and further they are willing to deposit the shareholder's shared certificate[s] as the corporation may require.
> 4. The dissenters further hereby notify the corporation that the dissenter's own estimate of the fair value of the dissenter's share is the sum of $19,018.40 per share.[588]

The merger proposal was adopted at the special meeting despite the Minority Shareholder's efforts. Subsequently, Mi-Tech delivered to each dissenting shareholder a Notice of Dissenter's Rights, which stated that any dissenting shareholder electing to demand payment pursuant to the IDR should provide notice of such to the company by means of the attached form on or before sixty days after the date of the Notice of Dissenter's Rights. Also, the Notice informed the dissenting shareholders that they must deposit their shares with the company

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583. *Id.* at 850-51.

584. *See id.* at 851. The Minority Shareholders were tenants in common of the shares held by the employee who had died. *See id.* at 850.

585. *Id.* at 851.

586. *Id.*

587. *Id.* at 850, 851.

588. *Id.* at 851.

on or before the expiration of the sixty day period.[589] In addition, Mi-Tech offered to exchange the Minority Shareholder's shares for $14,000 per share.[590] The Minority Shareholders did not demand payment or deposit their shares within the prescribed time period[591] and instead filed suit against the Majority Shareholders.[592] The Majority Shareholders filed their answer, claiming that the Minority Shareholder's exclusive remedy was the IDR statute.[593] The trial court granted the Majority Shareholder's motion for summary judgment without explanation or elaboration.[594]

On appeal, the Minority Shareholders contended their claims of breach of fiduciary duty and fraud were outside the scope of the IDR statute.[595] The *Settles* court noted that the Indiana Supreme Court's recent decision in *Fleming v. International Pizza Corp.*[596] held that the IDR statute "provides the exclusive remedy for minority shareholders challenging a proposed merger."[597] The Minority Shareholders contended that they declined to invoke their dissenter's rights and instead were pursuing individual fraud and breach of fiduciary duty claims against the Majority Shareholders.[598] However, the *Settles* court, in reviewing the complaint of the Minority Shareholders, came to the conclusion that the claims regarding fraud and breach of fiduciary duty were essentially claims regarding the fair value of the Minority Shareholder's share price in conjunction with the merger.[599] The *Settles* court held that the Minority Shareholders could not circumvent the remedy established by the legislature for valuing stock held by dissenting shareholders to a merger[600] simply by refusing to pursue their statutory remedies and filing common law claims for fraud and breach of fiduciary duty against the individuals controlling the corporation.[601]

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589. *See id.*

590. *Id.*

591. *Id.*

592. *See id.*

593. *See id.*

594. *See id.*

595. *Id.* at 852.

596. 676 N.E.2d 1051 (Ind. 1997).

597. *Settles*, 701 N.E.2d at 853 (citing *Fleming*, 676 N.E.2d at 1056). The IDR Statute provides in part:

> (a) A shareholder is entitled to dissent from, and obtain payment of the fair value of the shareholder's shares in the event of . . . [c]onsumation of a plan of merger to which the corporation is a party . . . . (b) A shareholder: (1) who is entitled to dissent and obtain payment for the shareholder's shares . . . may not challenge the corporate action creating . . . the shareholder's entitlement.

IND. CODE §§ 23-1-44-8(a), (c) (1998).

598. *Settles*, 701 N.E.2d at 853.

599. *Id.* at 853-54.

600. *Id.* at 852.

601. *Id.* at 854.

However, the *Settles* court went on to hold that, under the IDR statute, the dissenting shareholders were permitted to a judicial appraisal of the value of their shares.[602] The *Settles* court noted that a judicial appraisal was sufficiently comprehensive to incorporate any claims for wrongdoing brought by either the corporation or its shareholders in valuing just compensation to the dissenting shareholders.[603]

In reaching its decision, the *Settles* court relied heavily on the supreme court's decision in *Fleming*.[604] In *Fleming*, the plaintiff claimed dissenter's rights in connection with the sale by the sole majority shareholder of substantially all of the assets of the corporation.[605] In addition to claiming fair value for its shares, the *Fleming* plaintiff alleged that the majority shareholder had breached its fiduciary obligations to the plaintiff with regard to the asset sale. The *Fleming* court held that the IDR statute "'did not foreclose the ability of dissenting shareholders to litigate their breach of fiduciary duty or fraud claims *within the appraisal proceeding*.'"[606] The *Settles* court concluded that the trial court is authorized to create a comprehensive scope of valuation of claims for appraisers under the IDR statute in order to protect the rights of dissenting shareholders,[607] such as the Minority Shareholders. Thus, the court held that the IDR statute was the sole avenue of recourse for the Minority Shareholder's fraud and breach of fiduciary duty claims in conjunction with the merger and affirmed the trial court's grant of summary judgment.[608]

2. Direct Action Against the Corporation.—In *Barth v. Barth*,[609] ("*Barth III*") the court of appeals determined whether a minority shareholder in a corporation having a total of three shareholders could bring an action in its own name against the majority shareholder as opposed to a derivative action on behalf of the corporation. A minority shareholder of an electric company, Robert Barth ("Robert"), brought an action against the majority and controlling shareholder, Michael Barth ("Michael"), alleging that Michael had taken certain actions that had the effect of substantially reducing the value of Robert's shares of stock. The alleged actions included: (i) payment of excessive salaries to Michael and members of his immediate family; (ii) use of corporate employees to perform services on Michael's and his son's homes without proper compensation to the corporation; (iii) lowering dramatically dividend payments; and, (iv) appropriation of corporate funds for Michael's personal investments.[610] Michael

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602. *Id.*

603. *Id.* (citing Fleming v. International Pizza Supply Corp., 676 N.E.2d 1051, 1057 n.9 (Ind. 1997)).

604. *Fleming*, 676 N.E.2d at 1051.

605. *See Settles*, 701 N.E.2d at 855.

606. *Id.* (quoting *Fleming*, 676 N.E.2d at 1057 (emphasis supplied)).

607. *Id.* at 856.

608. *Id.*

609. 693 N.E.2d 954, 955 (Ind. Ct. App. 1998) [hereinafter *Barth III*].

610. *Id.*

and the corporation moved to dismiss for failure to state a claim "arguing that a derivative action suit was required to redress claims of this nature." [611] The trial court granted Michael's motion to dismiss and such ruling was reversed by the court of appeals.[612]

Upon transfer, the Indiana Supreme Court cited the general rule in Indiana that "shareholders of a corporation may not maintain actions at law in their own names to redress an injury to the corporation, even if the injury has the effect of impairing the value of their stock."[613] The supreme court explained that the general rule was established to prevent disregard for the corporate entity that would result if an individual lawsuit were permitted by disgruntled shareholders.[614] In addition, the general rule promotes the protection of all shareholders rather than allowing one shareholder to prejudice the interests of the other shareholders by receiving funds justly due the corporation.[615] Finally, the supreme court noted that the general rule protects corporate creditors by putting the proceeds of recovery back into the corporation.[616] The supreme court, however, indicated two reasons why the general rule will not always apply in the case of closely held corporation.

> "First, the shareholders in a close corporation stand in a fiduciary relationship to each other, and as such, must deal fairly, honestly, and openly with the corporation and with their fellow shareholders. Second, shareholder litigation in the closely-held corporation context will often not implicate the policies that mandate requiring derivative litigation when more widely-held corporations are involved."[617]

Thus, the supreme court held that a court has exempted a shareholder claim from the restrictions applicable to derivative actions if it determines that the lawsuit will not "(i) unfairly expose the corporation or the defendants to a multiplicity of actions, (ii) materially prejudice the interests of the creditors of the corporation, or (iii) interfere with a fair distribution of the recovery among all interested persons."[618] The supreme court then remanded the case back to the trial court.

On remand, the trial court held that, because the corporation had three

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611. *Id.*

612. *See* Barth v. Barth, 651 N.E.2d 291, 292 (Ind. Ct. App. 1995) [hereinafter *Barth I*].

613. *See Barth III*, 693 N.E.2d at 957 (citing Barth v. Barth, 659 N.E.2d 559, 560 (Ind. 1995) [hereinafter *Barth II*]).

614. *See id.* (quoting *Barth II*, 659 N.E.2d at 651).

615. *See id.* (citing *Barth II*, 659 N.E.2d at 561 (noting that the plaintiff shareholder receives adequate compensation by increasing its shares value when recovery is put back into the corporation)).

616. *Id.* (citing *Barth II*, 659 N.E.2d at 561).

617. *Id.* (quoting *Barth II*, 659 N.E.2d at 561).

618. *Id.* at 958 (quoting AMERICAN LAW INSTITUTE, PRINCIPALS OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS § 7.01(d) (1994)).

shareholders, one of which was not a party to Robert's action and would not be bound by any judgment in that case, by allowing Robert to proceed in a direct, rather than a derivative, action could expose Michael and the corporation to a multiplicity of lawsuits.[619] Reviewing the trial court's decision under an abuse of discretion standard, the *Barth III* court agreed that because there the remaining shareholder of The company had not joined in Robert's action, that third shareholder could bring a separate action against the corporation and Michael for its own damages to the price of its shares.[620]

Next, the *Barth III* court addressed whether Robert's lawsuit, if treated as a direct action, would prejudice creditors.[621] The *Barth III* court noted that Robert had petitioned the court for the corporation to pay damages to him, not its creditors; such a result, the *Barth III* court concluded, would be inherently prejudicial to creditors.[622] Finally, the court addressed whether Robert's action would result in a fair distribution of the corporation's assets.[623] The *Barth III* court agreed with the trial court that, because all damages would go to Robert, "the result . . . would constitute an unfair distribution of the assets of the corporation to only one of its shareholders."[624] Thus, the *Barth III* court concluded that the trial court did not abuse its discretion when it determined that Robert did not satisfy the supreme court's requirements set forth in *Barth II* for a direct action and affirmed the trial court's ruling.[625]

3. Foreign Corporations "Transacting Business" in Indiana.—In *Lackmond Products, Inc. v. Construction Supply, Inc.*,[626] the court of appeals addressed whether a Georgia corporation was "transacting business" in Indiana by selling goods to Indiana customers through the mail and by taking orders through an independent contractor located in Ohio. Lackmond sold products to Construction Supply, Inc. ("CSI"), an Indiana corporation, by taking orders in Georgia and shipping the goods to CSI at various locations in Indiana. When Lackmond filed suit against CSI for its alleged failure to pay for such goods, CSI moved to dismiss, arguing that Lackmond lacked the capacity to bring an action because it was a foreign corporation "transacting business" in Indiana without a certificate of authority.[627] The trial court dismissed the action and Lackmond appealed.

Under Indiana Code section 23-1-49-1(a),

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619. *See id.* at 958.

620. *Id.* (contrasting *W & W Equipment Co. v. Mink*, 568 N.E.2d 564, 570 (Ind. Ct. App. 1991), wherein the corporation only contained two shareholders and thus there was no potential for multiple shareholder suits).

621. *Id.*

622. *Id.*

623. *Id.* at 959.

624. *Id.*

625. *Id.*

626. 691 N.E.2d 494, 495 (Ind. Ct. App.1998).

627. *See id.*

> [a] foreign corporation may not "transact business" in Indiana until it obtains a certificate of authority from the secretary of state. Indiana Code [section] 23-1-49-2(a) further states that a foreign corporation transacting business in Indiana without a certificate of authority may not maintain a proceeding in any court in Indiana until it obtains a certificate of authority.[628]

However, the *Lackmond* court noted that, under Indiana Code section 23-1-49-1(b), certain activities do not constitute transacting business, including but not limited to "'(5) [s]elling through independent contractors[,] (6) [s]oliciting or obtaining orders, whether by mail or through employees or agent or otherwise, if the orders require acceptance outside Indiana before they become contracts . . . [, and] (11) [t]ransacting business in interstate commerce.'"[629] Finally, the *Lackmond* court noted that the allegation that a foreign corporation does not have the capacity to sue is an affirmative defense and the burden was upon CSI to support its contentions.[630]

The *Lackmond* court observed that CSI did not argue that Lackmond, by taking orders in Georgia and using an Ohio corporation to take orders, did not fall within the exceptions set forth in Indiana Code sections 23-1-49-1(b)(5), (6) and (11). Instead, CSI argued that Lackmond's contacts with Indiana were "'more regular, systematic or extensive than interstate sales activities described in' Indiana Code [section] 23-1-49-1(b).'"[631] The *Lackmond* court, however, stated that Lackmond's sales contracts with CSI were formed in Georgia because "Lackmond accepts [an] order by shipping the requested inventory to Indiana from its Georgia warehouse."[632] With these facts, the *Lackmond* court held that Lackmond's activities of filing customer-placed purchase orders sent to Lackmond's Georgia office by phone or facsimile specifically excluded from the definition of "transacting business" under Indiana Code section 23-1-49-1(b).[633] Thus, the court of appeals reversed the trial court's dismissal of Lackmond's action.

4. *Corporation's Liability for Acts of Employee.*—In *Coble v. Joseph Motors, Inc.*,[634] the court of appeals addressed whether a corporation would be deemed to have committed an intentional tort against an employee due to a

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628. *Id.* (citing IND. CODE §§ 23-1-49-1(1), -2(a) (1998)).

629. *Id.* at 495-96 (quoting IND. CODE §§ 23-1-49-1(b)(5), (6), (11) (1998)).

630. *Id.* at 496.

631. *Id.*

632. *Id.* The court also found CSI's offer of Lackmond sales invoices, which accompanied each shipment to CSI, to evidence that the purchase orders did not require acceptance outside Indiana before they became contracts unpersuasive, because the invoices were issued after Lackmond's acceptance of CSI's offer to purchase and therefore, after contraction formation. *Id.* at 496 n.3.

633. *Id.* at 496.

634. 695 N.E.2d 129, 133 (Ind. Ct. App. 1998).

supervisor's tortious acts. The plaintiff in *Coble* was injured in an accident at work that sliced off the tip of her finger.[635] The tip of the finger found its way to the human resources manager of the corporation, who used the severed fingertip as a prop in presentations to the employees regarding company safety. Coble brought a claim for emotional injuries against the corporation.[636] The trial court dismissed Coble's claim for want of jurisdiction based upon the exclusivity provision of the Worker's Compensation Act.[637]

On appeal, the employee argued that the corporation had committed an intentional tort against her, which was not covered by the Worker's Compensation Act.[638] The *Coble* court observed that, pursuant to the Supreme Court's decision in *Perry v. Stitzer Buick GMC, Inc.*,[639] "'tortious intent will be imputed to an employer that is a legal entity or artificial person where either (1) the corporation is the tortfeasor's alter ego or (2) the corporation has substituted its will for that of the individual who committed the tortious acts.'"[640] Thus, the *Coble* court concluded that in order for the corporation to be responsible for the human resource manager's intentional acts, the human resource manager must be the alter ego of the corporation or the corporation "must have intended the injury or actually known that the injury was certain to occur."[641] In reviewing the facts, the *Coble* court noted that the human resource manager was not an owner or controller of the corporation nor was there any evidence that the corporation intended to commit the torts against the employee or know that the injury was certain to occur. The human resource manager's actions were not undertaken pursuant to any policy of the corporation nor did management instruct the manager to display the employee's severed fingertip.[642] The employee argued that the corporation ratified the human resources manager's offensive acts by raising his salary subsequent to the incident.[643] However, the *Coble* court was not persuaded for two reasons: (i) the employee presented no evidence that the raise and the offensive conduct were linked, and (ii) the corporation subsequently fired the human resource manager in part because of this incident.[644] Thus, the *Coble* court affirmed the trial court's ruling.

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635. *Id.* at 131.

636. *Id.* at 131-32.

637. *See id.* at 132. This Article does not address the *Coble* court's discussion of issues regarding the Worker's Compensation Act.

638. *See id.* at 133.

639. 637 N.E.2d 1282 (Ind. 1994).

640. *Coble*, 695 N.E.2d at 134 (quoting *Perry*, 637 N.E.2d at 1287 (citations omitted in original)).

641. *Id.* at 134.

642. *See id.* at 134-35.

643. *See id.* at 135.

644. *Id.*

5. *Corporations Rights and Responsibilities with Regard to the Acts of Others.*—In *Summit Account & Computer Service, Inc. v. RJH of Florida, Inc.*,[645] the court of appeals determined whether a corporate successor in interest may be awarded punitive damages and attorney's fees for damages incurred by its predecessor pursuant to the Indiana Criminal Conversion Statute.[646] In *Summit*, a leasing company brought an action against a collection agency for conversion of property under Indiana Code section 35-43-4-3, a proven violation of which permits a recovery of treble damages, costs of the action and reasonable attorney's fees.[647] The trial court awarded the leasing company treble damages, costs and attorney's fees and defendants appealed.[648]

On appeal, the collection agency argued that the leasing company's successor in interest (the "successor corporation"), could not recover for damages incurred by the leasing company because, under the ruling of *Hart Conversions, Inc. v. Pyramid Seating Co.*,[649] such tort claims are not assignable.[650] In *Summit*, the leasing company had sold all of its assets, including its claims against the collection agency, to a third party that in turn sold the assets to the successor corporation.[651] One individual was the sole shareholder, director and officer of all three corporations, and the corporations conducted business of the same nature from the same place.[652] Citing the court of appeals' decision in *Mishawaka Brass Manufacturing v. Milwaukee Value Co.*,[653] the trial court held that the successor corporation was a direct continuation of the ownership and operations of the leasing company with only a change of name.[654] Under the ruling in *Mishawaka Brass*, "'a direct continuation of the ownership and operations of the first corporation,' with only a change of name 'will not cut off liability to a creditor of the first corporation.'"[655] Applying this rule, the *Summit* court

645. 690 N.E.2d 723, 724 (Ind. Ct. App. 1998).

646. IND. CODE § 35-43-4-3 (1998).

647. *Summit Account & Computer Serv.*, 690 N.E.2d at 725-26. *See also* IND. CODE § 34-1 (1998) (providing for civil actions against persons who violate Indiana Code section 35-43-4-3, and providing what damages are available in such suits). This Article focuses on the issue of damages available under this statute to a corporate successor in interest.

648. *See Summit Account & Computer Serv.*, 690 N.E.2d at 726.

649. 658 N.E.2d 129 (Ind. Ct. App. 1955).

650. *See Summit Account & Computer Serv.*, 690 N.E.2d at 728.

651. *See id.*

652. *See id.*

653. 444 N.E.2d 855 (Ind. Ct. App. 1983).

654. *See Summit Account & Computer Serv.*, 690 N.E.2d at 728.

655. *Id.* (quoting *Mishawaka Brass*, 444 N.E.2d at 858).

affirmed the trial court's determination that the successor corporation was a direct continuation of its predecessors and should have the same rights and liabilities thereof.[656]

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656. *Id.* A third case addressing this topic but not discussed in this survey is *Wabash Grain, Inc. v. Smith*, 700 N.E.2d 234, 235 (Ind. Ct. App. 1998). In *Wabash Grain*, the court of appeals addressed whether an action filed against a related corporation in federal court would toll the statute of limitations with regard to a subsequent action against a related corporation in state court. The *Wabash Grain* court noted that although both corporations were controlled by the same individual, each corporation is a distinct legal entity under the law; therefore, an action against one corporation will not toll the statute of limitations against an affiliated corporation. *Id.* at 240. The plaintiff also argued that equitable tolling should apply given that the corporation it sued first in federal court was controlled by or controlled the affiliated corporation it sued second in state court. *See id.* However, the *Wabash Grain* court noted that the plaintiff presented no evidence to establish that either corporation "'so ignored, controlled or manipulated'" the other, or "'that the misuse of the corporate form would constitute a fraud or promote in justice.'" *Id.* (quoting Winkler v. V.G. Reed & Sons, Inc., 638 N.E.2d 1228, 1231 (Ind. 1994)).

CONTRACT DAMAGES AS SUBSTITUTE FOR FULL PERFORMANCE

JAMES P. NEHF*

One of the first lessons contract students learn is that a party to a contract has a choice between two courses of action. The party can either perform the contract according to its terms or pay damages for not performing. This concept is usually stated in a neutral, nonjudgmental manner, as if it does not matter which course is chosen. Indeed, modern contracts textbooks teach that there is nothing morally wrong with breaching contracts; in some instances it may even be economically efficient to breach.[1] One of the principal justifications for this counterintuitive notion is found in the theory of damages: So long as the breaching party is willing to pay full compensation for the breach, the other party will be "made whole" and the nonperformance will be remedied entirely.[2] In theory, the payment of damages is the monetary equivalent of full performance.

Practicing lawyers and their clients, of course, know differently. The successful prosecution of a breach of contract claim rarely means that the plaintiff has been "made whole." The plaintiff may rejoice at first upon hearing that the case on the merits is strong, only to despair when told about the difficulties of obtaining full compensation and the expenses that must be borne by the plaintiff to prosecute the action. As it turns out, the payment of damages seldom, if ever, even approximates the equivalent of contract performance.

The problem of obtaining full compensation from the breaching party, or as close to full compensation as possible, is a vexing one for lawyers who litigate contract claims. The client may think that he or she has been harmed in a myriad of ways, but some of the injuries may be speculative, intangible, difficult to quantify in dollar amounts, or simply unrecoverable in contract actions. The Indiana Court of Appeals recently reaffirmed, for example, longstanding rules that damages for emotional distress[3] and lost reputation[4] are not compensable under a contract theory, even though the injuries are very real in the eyes of the

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* Professor of Law, Indiana University School of Law—Indianapolis. Law student Kandel Eaton provided valuable research assistance in the preparation of this Article. A prior version of this paper was presented at an Indiana Continuing Legal Education Foundation seminar in Indianapolis, Indiana. James Nehf, *Full Compensation from the Breaching Party, presented at* The "Unbreakable" Contract: Myth v. Reality, Aug. 24, 1994.

1. *E.g.*, JOHN P. DAWSON ET AL., CASES AND COMMENT ON CONTRACTS 31 (6th ed. 1993).

2. *See* RESTATEMENT (SECOND) CONTRACTS, Introductory Note and Reporter's Note, ch. 16 (1981) ("[T]he principal purpose of the rules relating to breach is to place the injured party in as good a position as he would have been in had the contract been performed.").

3. Holloway v. Bob Evans Farms, Inc., 695 N.E.2d 991 (Ind. Ct. App. 1998) (holding that distress damages are not available in contract to plaintiff who found a half-cooked worm on her fork while eating at restaurant).

4. Wells v. Stone City Bank, 691 N.E.2d 1246 (Ind. Ct. App. 1998) (holding that bank that wrongfully dishonored checks not liable for lost business reputation or profits resulting from "loss of face" in industry; reputation losses only compensable in actions for libel, slander, abuse of process, malicious prosecution, and third-party contract interference).

plaintiff. Lost profits and other consequences of the breach may be difficult to prove. Moreover, most lawyers want to be paid for their work, and under the American Rule even a successful plaintiff in a breach of contract action will have to bear her own legal expenses.[5] The costs of litigation may exceed or substantially reduce any expected recovery, leaving the client with the disheartening choice of either compromising a valid claim by accepting a partial settlement, or prosecuting to the end and winning a pyrrhic victory.

The prospect of not recovering for these types of losses motivates lawyers to seek additional, sometimes creative, ways of obtaining greater damage recoveries that may more closely approximate the monetary equivalent of performance, and thus make the client's case worth pursuing. This Article discusses some of the things lawyers can do, both in the contract drafting stage and in the course of litigation, to increase the chances of obtaining the monetary equivalent of performance from the breaching party. It begins with a review of the basic measure of damages for breach of contract in Indiana, and discusses some of the problems generated by those rules. The Article then examines five ways of enhancing damage recoveries to overcome some of these problems: expansive approaches to consequential damage recoveries, creative arguments for punitive damage awards, tactics for obtaining attorney's fees, ways to claim prejudgment interest, and aggressive use of liquidated damages provisions.

I. Compensatory Damages for Breach of Contract

When a contract is breached, the traditional remedy is an award of money damages. A court will order specific performance of the contract only in the unusual case where an award of damages would be inadequate, causing the aggrieved party irreparable injury if performance is not mandated. When a seller of real property breaches a land sale contract, the buyer might obtain specific performance by arguing that the land is unique and cannot be replaced at any price.[6] Occasionally, the buyer of goods or services can also secure an order of specific performance by showing that the goods or services are unique and cannot be obtained elsewhere.[7] The general presumption applied in the vast majority of contract actions, however, is that the aggrieved party will be limited to a claim for compensatory damages.

The way in which courts usually fix compensation is by awarding expectancy

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5. *See infra* notes 95-96 and accompanying text.

6. Land is generally regarded as unique, so the purchaser can almost routinely secure a decree of specific performance. *See* North v. Newlin, 416 N.E.2d 144 (Ind. Ct. App. 1981).

7. *See, e.g.*, Brown County Art Guild, Inc. v. Mann, 430 N.E.2d 1181 (Ind. Ct. App. 1982) (addressing contract for sale of art work). Section 2-716 of the Uniform Commercial Code provides that "specific performance may be declared where goods are unique or in other proper circumstances." U.C.C. § 2-716. *See also* Massachusetts Mut. Life Ins. Co. v. Associated Dry Goods Corp., 786 F. Supp. 1403 (N.D. Ind. 1992) (ordering anchor store in shopping mall to honor lease because irreparable injury would result if the store closed).

damages.[8] This requires the court to create a hypothetical situation. The court attempts to reconstruct the financial position the aggrieved party would have occupied if the contract had been performed, and compares it to the financial position following a breach. The difference between the two, in dollar amount, is the damage award. The aggrieved party is thus, in theory, placed in the same position it would have occupied had the contract not been breached.[9] This is frequently stated as awarding "lost bargain" damages or giving the aggrieved party the "benefit of the bargain."[10]

The method for computing the lost bargain in dollars will depend on the circumstances of each case, but courts have developed general rules. One typical approach is a market-based computation. The court compares the market value that the goods/land/services would have had if the contract had been performed, with the market value of the goods/land/services after nonperformance, i.e., on the date of the breach. This is designed to give the aggrieved party the same amount of wealth or net worth as was promised in the agreement. The market-based method is often used in land sale cases where the buyer has breached. The seller is given the difference between the contract price and the market value of the land.[11] It may also be useful in construction cases when the builder has breached. The owner is given the difference between the value the property would have had if the construction had been done properly, compared with the value of the property in its condition on the date of nonperformance.[12] Proving market values may require estimates from real estate appraisers or other expert witnesses.[13] The market-based method is also endorsed by the UCC when the buyer or seller breaches a contract for the sale of goods. The damages are the difference between the contract price and market price on the date of breach.[14]

The market measure of damages is useful in some cases, but it can be unsatisfactory in the eyes of the aggrieved party. In a land sale contract, for instance, the market value of the real estate on the date of breach might be the

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8. *See* Holloway v. Bob Evans Farms, Inc., 695 N.E.2d 991, 995 (Ind. Ct. App. 1998) ("plaintiff is not entitled to be placed in a better position than he would have been had the breach not occurred").

9. *See* David H. Vernon, *Expectancy Damages for Breach of Contract: A Primer and Critique*, 1976 WASH. U. L.Q. 179.

10. *See* Hudson v. McClaskey, 597 N.E.2d 308, 309 (Ind. 1992).

11. *See* Annon II, Inc. v. Rill, 597 N.E.2d 320, 326 (Ind. Ct. App. 1992); Arlington State Bank v. Colvin, 545 N.E.2d 572, 575 (Ind. Ct. App. 1989).

12. *See, e.g.*, Pierce v. Drees, 607 N.E.2d 726 (Ind. Ct. App. 1993); Gough Constr. Co. v. Tri-State Supply Co., 493 N.E.2d 1283 (Ind. Ct. App. 1986).

13. There are three accepted methods of determining a property's fair market value: (1) the current cost of reproducing the property less depreciation; (2) the value indicated by recent sales of comparable properties in the market; and (3) the value that the property's net earning power will support based upon the capitalization of net income (the "income approach"). Courts may combine all three approaches to determine market value. *See Annon II*, 597 N.E.2d at 326-27; Ohio Cas. Ins. Co. v. Ramsey, 439 N.E.2d 1162, 1167 (Ind. Ct. App. 1982).

14. *See* U.C.C. § 2-708(1) (seller's damages); § 2-713(1) (buyer's damages).

same as the contract price. The damage computation may then be zero, because the seller's net worth is no worse after the breach. Yet the seller is still in possession of land she had expected to sell, and she must now wait for another buyer.[15] An example from a construction contract is *Willie's Construction Co. v. Baker*.[16] The Bakers contracted to have their new home built with one hundred inch basement ceilings, twelve inches higher than the norm, at an extra cost of only $414. The builder constructed the basement with the standard height ceilings, and the Bakers sued for breach of contract. Evidence showed that the market value of the house was not reduced at all by the lower ceiling height, so the market measure of damages was zero.[17]

The Bakers successfully argued, however, that the court should use an alternative approach—the cost of conforming the performance to the contract specifications, which came to $24,000. This illustrates the second general method courts may use in assessing contract damages—the "cost-of-cure" computation,[18] in which the court awards the price of repairing or replacing the property or services.[19] This may be the only way to provide adequate compensation to the plaintiff. In *Willie's Construction,* the court observed that the fair market value of the home did not necessarily reflect the value of the deep basement to the Bakers.[20] It was difficult to put a valuation on that feature because the Bakers requested it as a matter of personal taste, not because it would increase the value of their house.[21] The only way to give them the monetary equivalent of full performance was to award $24,000 damages so they could have the ceilings raised.

The cost-of-cure computation can be a useful tool for plaintiffs in contract actions because it enables them to purchase the goods or services that were bargained for. But a court will not use this approach if it is concerned that the plaintiff is getting a windfall by taking the money and not doing the repair or replacement. In *Willie's Construction*, for example, there was no guarantee that the Bakers would use the $24,000 to deepen the basement. They could keep the $24,000, and their net worth would be increased by that amount. The plaintiffs would be overcompensated and receive more than the benefit of the bargain.

The cost-of-cure remedy is used often in Indiana, and was applied recently

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15. *See* Stoneburner v. Fletcher, 408 N.E.2d 545, 551 (Ind. Ct. App. 1980) (refusing to use market measure because damages would be zero).

16. 596 N.E.2d 958 (Ind. Ct. App. 1992).

17. *See id.* at 960.

18. *See* Clark's Pork Farms v. Sand Livestock Sys., 563 N.E.2d 1292, 1297 (Ind. Ct. App. 1990). This damage computation method is also endorsed in section 348 of the second Restatement of Contracts. RESTATEMENT (SECOND) OF CONTRACTS § 348 (1981).

19. This "cost of cure" alternative approach is also reflected in the UCC provisions allowing an aggrieved seller to resell the goods and recover the difference between the resale price and the contract price, U.C.C. § 2-706, and an aggrieved buyer to recoup the cost of "cover" when he buys the goods from someone else after the breach, U.C.C. § 2-712.

20. *Willie's Constr.*, 596 N.E.2d at 961.

21. *See id.*

in *Bee Window, Inc. v. Stough Enterprises, Inc.*,[22] another situation in which the damage award exceeded the contract price. Bee Window had agreed to install windows in a commercial building for $37,585. The windows leaked periodically over the next ten years, and Bee Window tried several times but failed to fix the problem. Finally, the owner brought suit to recover the cost of installing new windows from a different vendor, estimated to be over $48,000. The Court of Appeals affirmed the trial court's award for the full replacement cost, even though it was higher than the original contract price[23] and the owner had the use of the windows, albeit in a defective state, for more than ten years.

The test Indiana courts have devised to limit the cost-of-cure formulation is to ask whether the defective performance can be remedied without unreasonable "economic waste," i.e., whether the cure would require substantial reconstruction or excessive costs.[24] This is a flexible standard, of course, and economic waste is not well defined in the case law. The court in *Willie's Construction* felt that the amount of basement reconstruction, which might include razing the entire house and refitting utility connections, did not amount to excessive waste.[25] The result was that the builder had to make a $24,000 damages payment for a job that would only have cost a small fraction of that amount if it had been done in the first instance. At the other end of the spectrum is *City of Anderson v. Sailing Concrete Corp.*,[26] where the court refused to award $590,000 needed to repair the plaintiff's land when the value of the land after repair would only have been $270,000. It would constitute economic waste to require such a large payment for so little benefit.[27]

One of the unstated reasons courts tolerate the risk of overcompensating the plaintiff with a generous cost-of-cure measure of damages may be that many of the plaintiff's injuries are not compensable at all. Even if the Bakers did not use the $24,000 to raze their house, for example, they still might not have received a windfall. They had to pay their attorney through a trial and appeal. They had to live in a house with lower basement ceilings for more than three years while the case was being decided, and they may have to live with this deficiency much longer if they choose not to raise the ceilings or sell the home. They probably endured some emotional stress and aggravation throughout the proceedings, and devoted much time and energy, possibly taking time off work, to prosecute the

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22. 698 N.E.2d 328 (Ind. Ct. App. 1998).

23. *Id.* at 330.

24. *See* Clark's Pork Farms v. Sand Livestock Sys., 563 N.E.2d 1292, 1297 (Ind. Ct. App. 1990); Sanborn Elec. Co. v. Bloomington Athletic Club, 433 N.E.2d 81, 89 (Ind. Ct. App. 1982).

25. Economic waste is not well defined in Indiana. Other jurisdictions have described it as "the destruction of usable property," Gold Rush Inv., Inc. v. G.E. Johnson Constr. Co., 807 P.2d 1169, 1174 (Colo. Ct. App. 1990); "substantial undoing of a contractor's work," City of Charlotte v. Skidmore, Owings & Merrill, 407 S.E.2d 571, 581 (N.C. Ct. App. 1991); and a situation where the cost of repair exceeds the original cost of construction, Johnson v. Garages, Etc., Inc., 367 N.W.2d 85, 86 (Minn. Ct. App. 1985).

26. 411 N.E.2d 728 (Ind. Ct. App. 1981).

27. *See id.* at 734.

action. They may have even been planning to use the deeper basement for some particular purpose that had to be abandoned because of the defective construction. Moreover, if they choose to use the money to have the house razed and rebuilt, they will either have to move out or live in a construction zone for several months while the work is being done.

None of these injuries would have occurred if performance had been made as promised, yet most are probably not compensable under traditional contract rules. While the construction contract did provide for attorney's fees if the builder had to sue the Bakers, it did not provide for the reverse, so the Bakers had to pay their lawyer. Psychological injuries—living in a shallow basement, enduring emotional stress, and putting up with subsequent construction headaches—would likely be viewed as emotional harm not compensable unless the defendant acted fraudulently or the breach was accompanied by physical injury.[28] Any injuries resulting from not being able to use the basement as planned might be considered unforeseeable consequential damages.

The Bakers were fortunate that the cost-of-cure measure was high enough to offset some of these noncompensable types of harm. Most plaintiffs do not find the damages award so generous. The rest of this Article discusses ways to give the nonbreaching party a better chance at more complete recovery from the contract breacher.

II. Consequential Damages

The measure of damages in contract cases is the loss actually suffered as a result of the breach.[29] Not all of the actual loss is compensable, however. The plaintiff must overcome three hurdles: (1) the damage must be the natural and proximate consequence of the breach,[30] (2) it must have been within the contemplation of the parties when the agreement was reached,[31] and (3) it must be proved with reasonable certainty.[32] In essence, the Indiana courts follow the rule of *Hadley v. Baxendale*,[33] awarding only those damages that may reasonably be supposed to have been in the contemplation of the parties at the time the

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28. *See supra* note 3; *see also* Captain & Co. v. Stenberg, 505 N.E.2d 88, 100 (Ind. Ct. App. 1987); Little v. Williamson, 441 N.E.2d 974, 975 (Ind. Ct. App. 1982). In addition, a plaintiff may recover emotional distress damages where "the defendant by extreme and outrageous conduct intentionally or recklessly caused severe emotional distress . . . or where the conduct causing the injury was inspired by fraud malice, or like motives." Tacket v. General Motors Corp., 818 F. Supp. 1243, 1248 (S.D. Ind. 1993) (citations omitted).

29. *See* Holloway v. Bob Evans Farms, Inc., 695 N.E.2d 991, 995 (Ind. Ct. App. 1998); *see also* Burleson v. Illinois Farmers Ins. Co., 725 F. Supp. 1489, 1495 (S.D. Ind. 1989); Ethyl Corp. v. Forcum-Lannon Assoc., Inc., 433 N.E.2d 1214, 1221 (Ind. Ct. App. 1982).

30. *See* Finley v. Chain, 374 N.E.2d 67, 76 (Ind. App. 1978).

31. *See* Strong v. Commercial Carpet Co., 322 N.E.2d 387, 392 & n.2 (Ind. App. 1975).

32. *See* I.C.C. Protective Coatings, Inc. v. A.E. Staley Mfg. Co., 695 N.E.2d 1030, 1037 (Ind. Ct. App. 1998).

33. 156 Eng. Rep. 145 (Ex. D. 1854).

contract was entered, as the probable result of its breach.[34]

The first hurdle—proximate causation—usually creates few difficulties. It essentially requires a showing that the breach was an actual contributing cause of the loss (i.e., causation in fact) with the losses flowing "directly and naturally from the breach."[35] If it appears that the loss was in fact caused by the breach, but it was a remote consequence, the proximate causation inquiry melts into the second requirement—that the loss be reasonably contemplated as a probable result of the breach.[36] This is the issue given the most extensive treatment in the courts, and is the heart of *Hadley*. For example, in one case, recovery was denied to an individual who claimed damages from sickness and loss of employment when his insurance company denied payment under a fire insurance policy.[37] The court held that the injuries were too remote and thus not in the contemplation of the parties when they signed the home insurance contract.[38]

In other cases involving fire insurance, however, claimants have fared better. In one action, an individual sought damages arising from foreclosure on his mortgage after the insurance company refused to pay the claim.[39] The court stated that this financial loss was directly related to the company's refusal to pay, and thus was more likely to have been within the contemplation of the parties as a probable consequence of a breach.[40] In another decision, *Indiana Insurance Co. v. Plummer Power Mower*,[41] a business claimed $90,000 reimbursement for costs incurred in defending legal actions filed against it by creditors after the business location had burned down. The court upheld much of the award, stating that when a business owner contracts for insurance, he expects prompt payment

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34. *See I.C.C. Protective Coatings*, 695 N.E.2d at 1037; *Strong*, 322 N.E.2d at 392 n.2.

35. Sammons Communications of Ind., Inc. v. Larco Cable Constr., 691 N.E.2d 496, 498 (Ind. Ct. App. 1998).

36. *See Strong*, 322 N.E.2d at 392 & n.2.

37. Meridian Mut. Ins. Co. v. McMullen, 282 N.E.2d 558 (Ind. App. 1972).

38. *Id.* at 566.

39. Burleson v. Illinois Farmers Ins. Co., 725 F. Supp. 1489, 1489-90 (S.D. Ind. 1989).

40. *Id.* at 1496. The court ultimately denied recovery for consequential damages, however, on the ground that damages were limited to the maximum amount of the insurance policy. *Id.* at 1497-98. The Indiana Court of Appeals subsequently held that consequential damages in an insurance case can exceed the policy limits. *See* Indiana Ins. Co. v. Plummer Power Mower & Tool Rental, Inc., 590 N.E.2d 1085 (Ind. Ct. App. 1992). Some commentators disagree and argue that no consequential damages should be recoverable if the insurer denies coverage in good faith. *See* ROBERT E. KEETON & ALAN I. WIDISS, INSURANCE LAW—A GUIDE TO FUNDAMENTAL PRINCIPLES, LEGAL DOCTRINES AND COMMERCIAL PRACTICES § 7.9(d) (1988). Although *Plummer Power Mower* has not been overruled on this point, the Indiana Supreme Court, in denying punitive damages absent bad faith denial of benefits, has stated that an insurer has a "right to disagree" and is "'permitted to dispute liability in good faith because of the social costs of a rule which would make claims nondisputable.'" Erie Ins. Co. v. Hickman, 622 N.E.2d 515, 520 (Ind. 1993) (quoting Vernon Fire & Cas. Ins. Co. v. Sharp, 349 N.E.2d 173, 180 (Ind. 1976)). *See infra* note 76 and accompanying text.

41. 590 N.E.2d 1085 (Ind. Ct. App. 1992).

so he can resume operations.[42] Delayed payment will "undoubtedly" result in the failure of the business, and the owner will not be able to generate enough income to pay creditors.[43] In the words of Judge Conover, "The likelihood of such damages is only unforeseeable to unreasonably narrow-minded insurers."[44]

Proving that the losses were reasonably contemplated at the time of contracting, as a probable result of the breach can be difficult. The case usually turns on the court's view of the expectations of the parties when the contract was made. Unfortunately, most contracting parties (and their lawyers) do not think much about the consequences of breach during the contract formation stages. Once litigation ensues, the plaintiff's lawyer frantically tries to find some evidence that the defendant knew, or had reason to know, of the plaintiff's particular circumstances and needs at the time the deal was made. Often, the initial correspondence between the parties will give some indication of the plaintiff's needs. But typically, the only evidence is testimony about what the plaintiff told or showed the defendant about his business or his particular reasons for entering into the contract. These statements will usually be contradicted by the defendant, and the plaintiff might not carry his burden of proof. As a precautionary measure, though at the risk of over-lawyering, it may be advisable to document the expectations of the client during the pre-contract discussions, and make sure the other party is made aware of the client's circumstances. Typically, the "recital" or "whereas" clauses at the beginning of a contract are an appropriate place to insert these contractual expectations.

If the causation and foreseeability problems can be solved, the third hurdle the plaintiff must overcome is establishing that the damages are supported by more than speculation or conjecture. Indiana courts will look for objective evidence. In *Showalter, Inc. v. Smith*,[45] the Smith family had contracted to sell several summer camps to Showalter. Following breach of the agreement by Showalter, the Smiths sought, inter alia, about $29,000 in consequential damages for interest paid on outstanding debts that would have been retired had Showalter complied with the terms of the purchase agreement. Gary Smith testified that he would have used the sale proceeds to pay off the debts, and the trial court awarded the damages based on this uncontradicted evidence alone.[46] The court of appeals reversed, however, concluding that it could "only speculate as to whether Smith would have actually paid off these debts with the proceeds."[47] Judge Shields, in dissent, accused the majority of placing its judgment of Smith's

42. *Id.* at 1092.

43. *See id.*

44. *Id.* Judge Conover continued, "Simply put, the insurer cannot look at an insured's loss of livelihood and loss of home, shrug its shoulders, and hide behind the fact that in made an 'honest mistake.' Delay, whether in good or bad faith, has clearly foreseeable consequences." *Id.* at 1092 n.6. The court denied recovery for some of the losses, however, because they did not appear to be caused by the late payment. *Id.* at 1092.

45. 629 N.E.2d 272 (Ind. Ct. App. 1994).

46. *See id.* at 276.

47. *Id.*

credibility above that of the trial court.[48] She would have affirmed the award as supported by competent evidence.[49]

Damages need not be proved with absolute or mathematical certainty.[50] Evidence is sufficient so long as it enables the jury to make a "fair and reasonable finding" as to the proper damages.[51] The problem is most acute when the plaintiff seeks lost profits resulting from the breach. A claim for lost profits almost always provokes a challenge that the plaintiff is engaging in speculation. The problem is compounded when the plaintiff is claiming that it would have earned profits from business activities that never took place. Indiana courts are not hostile to claims of lost profits, though some objective evidence must be presented. "Consequential damages may include lost profits, providing the evidence is sufficient to allow the trier of fact to estimate the amount with a reasonable degree of certainty and exactness."[52] The trial court has great discretion in determining whether to submit the question of lost profits to the jury, and the fact finder has broad discretion in determining the amount.[53] Moreover, where there is any doubt about the exact proof of damages, the uncertainty will be resolved against the wrongdoer.[54]

There are limits, of course. One may not recover for "loss of face" in the industry or loss of goodwill.[55] The injury must arise directly from the breach of performance at issue. This can be problematic in many contract situations, particularly employment agreements when the employee breaches a covenant not to compete, as illustrated recently in *Turbines, Inc. v. Thompson*.[56] Thompson left the company to start his own engine repair business and then began soliciting the company's customers in violation of a one-year non-compete clause. The trial court found that the company did not prove lost profits even though Thompson had done substantial business with company customers after he left.[57] In affirming, the appellate court stated that it "'could not be sure whether the decline in [Turbines'] revenues was merely cyclical or was the product of Thompson's competition.'"[58] It was not enough to show the gross or net profits

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48. *See id.* at 277 (Shields, J., dissenting in part).

49. *Id.*

50. *See* I.C.C. Protective Coatings, Inc. v. A.E. Staley Mfg. Co., 695 N.E.2d 1030, 1037 (Ind. Ct. App. 1998); Turbines, Inc. v. Thompson, 684 N.E.2d 254, 258 (Ind. Ct. App. 1997); Farm Bureau Mut. Ins. Co. v. Dercach, 450 N.E.2d 537, 541 (Ind. Ct. App. 1983).

51. *I.C.C. Protective Coatings*, 695 N.E.2d at 1037; Jerry Alderman Ford Sales, Inc. v. Bailey, 291 N.E.2d 92, 106 (Ind. App. 1972).

52. Insul-Mark Midwest, Inc. v. Modern Materials, Inc., 594 N.E.2d 459, 466 (Ind. Ct. App. 1992), *aff'd in part and rev'd in part on other grounds*, 612 N.E.2d 550 (Ind. 1993).

53. *See id.* at 467 (citing CORBIN ON CONTRACTS 145-46 (1964)).

54. *See* Pepsi-Cola Co. v. Steak 'N Shake, Inc., 981 F. Supp. 1149, 1160 (S.D. Ind. 1997).

55. *See* Indiana & Mich. Elec. Co. v. Terre Haute Indus., Inc., 507 N.E.2d 588, 606-07 (Ind. Ct. App. 1987).

56. 684 N.E.2d 254 (Ind. Ct. App. 1997).

57. *See id.* at 258-59.

58. *Id.* at 257 (quoting trial judge).

Thompson had earned from his dealings with Turbines' customers; the company had to prove that its own reduced profits were attributable to Thompson's actions and not some other cause.[59]

The plaintiff is not likely to recover for losses attributable to contracts other than the one broken, i.e., contracts to which the defendant was not himself a party. One notable exception, however, is the *Insul-Mark* case.[60] Insul-Mark had contracted to purchase specially coated screws to be used in roofing materials. Insul-Mark was a distributor and intended to resell the screws to other buyers; Modern Materials apparently knew this. When Insul-Mark's buyers complained that the screws did not resist rusting as promised, Insul-Mark sued Modern Materials to recover, inter alia, damages for lost profits on the resale contracts, as well as lost profits on future contracts with the same resale customers and other potential buyers.[61] Insul-Mark introduced the testimony of an economist who explained how the company would have made profits from future sales if the coating had performed as promised, essentially attempting to quantify the "ripple effects" of the breach.[62] Modern Materials did not challenge the availability of lost profits on the particular resale arrangements immediately connected with its contract. It moved for summary judgment, however, with respect to all other claims for lost future profits to these resale customers and others.[63]

The court of appeals reached a compromise solution. It held that summary judgment was appropriate on the claims for lost future profits from customers who had not contracted to receive the defective screws.[64] These were deemed the equivalent of claims for loss of goodwill and business reputation. Summary judgment was reversed, however, on claims for future profits that might have been earned from the customers who had contracted to receive the screws.[65] The court would permit the trier of fact to decide whether Insul-Mark would likely have earned future profits from these customers in subsequent agreements, not only from the resale contracts connected with the screws at issue.

Insul-Mark is a good case for plaintiffs because it allows for the recovery of lost profits beyond those immediately expected from the contract that was breached. The key factor was the "objective" evidence of the plaintiff's economist, who quantified a continuing relationship between Insul-Mark and its customers. The lesson for plaintiffs' lawyers is to seek evidence of specific losses that can be directly traced to the contract, even if the losses do not arise from the contract in the first instance. If the evidence makes the losses appear to have resulted more from the expected contract performance than the general loss of goodwill or business reputation, the court may allow the fact finder to

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59. *See id.*

60. Insul-Mark Midwest, Inc. v. Modern Materials, Inc., 594 N.E.2d 459 (Ind. Ct. App. 1992), *aff'd in part and rev'd in part on other grounds*, 612 N.E.2d 550 (Ind. 1993).

61. *See id.* at 466.

62. *See id.* at 467.

63. *See id.* at 466.

64. *Id.* at 468.

65. *Id.* at 467-68.

bring it into the damage computation.

Plaintiff's lawyers need to be careful, however, in pleading their case. The Seventh Circuit, in the highly publicized case *Creative Demos, Inc. v. Wal-Mart Stores, Inc.*,[66] reaffirmed Indiana law that lost profits are not recoverable under a promissory estoppel theory, regardless how certain the proof.[67] While profits can be sought for breach of the contract itself, if the prevailing theory is promissory estoppel, the remedy is limited to losses incurred in relying on the promise. This will not ordinarily include expectancy damages like lost profits.[68]

III. Punitive Damages

For years, Indiana courts struggled to draw the line between breaches of contract that will support a punitive damages award and those that will not. Under a long line of cases, if the defendant not only breached the contract but acted with "malice," or engaged in conduct that was "tortious in nature"[69] or "oppressive," punitive damages could be awarded.[70] As the lower courts began to expand the reach of this doctrine to more and more "tort-like" conduct, the supreme court put on the brakes. In *Travelers Indemnity Co. v. Armstrong*,[71] the court heightened the burden of proof, requiring the plaintiff to prove malice, tort-like behavior or oppressive conduct by "clear and convincing evidence."[72] In 1993 the court went further and declared in *Miller Brewing Co. v. Best Beers of Bloomington, Inc.*,[73] that punitive damages would only be available when the plaintiff proves an actual tort.[74] Breach of contract coupled with malice, tort-like conduct or oppressive behavior, would not be enough.

Thus, the black-letter law in Indiana is that punitive damages are not available for breach of contract.[75] That will not stop lawyers from seeking punitive damages, however, when a contract has been breached and the client has been wronged. The focus of the case will now shift to proving the elements of a recognized tort, or arguing for the creation of a new tort.

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66. 142 F.3d 367 (7th Cir. 1998).

67. *Id.* at 369.

68. *See id.*

69. *See* Utopia Coach Corp. v. Watherwax, 379 N.E.2d 518 (Ind. Ct. App. 1978).

70. *See* Art Hill Ford, Inc. v. Callender, 423 N.E.2d 601 (Ind. 1981); Arlington State Bank v. Colvin., 545 N.E.2d 572 (Ind. Ct. App. 1989). The plaintiff must provide evidence that the defendant's conduct was "inconsistent with the hypothesis that the conduct was the result of mistake of law or fact, honest error of judgment, overzealousness, mere negligence or other such noniniquitous human failing." Dow Chem. v. St. Vincent's Hosp., 553 N.E.2d 144, 150 (Ind. Ct. App. 1990).

71. 442 N.E.2d 349 (Ind. 1982).

72. *Id.* at 362-63.

73. 608 N.E.2d 975 (Ind. 1993).

74. *Id.* at 984.

75. Creative Demos, Inc. v. Wal-Mart Stores, Inc., 142 F.3d 367 (7th Cir. 1998); USA Life Ins. Co. of Ind. v. Nuckolls, 682 N.E.2d 534 (Ind. 1997).

The Indiana Supreme Court adopted the latter approach in 1993 when it held in *Erie Insurance Co. v. Hickman*,[76] that it would, for the first time, recognize the tort of bad faith breach of an insurance contract. Realizing that *Best Beers* had removed punitive damages from breach of contract claims, it followed the view of most states and created a new tort. In doing so, however, it set out a general standard for determining when a tort has been committed. There must be a breach of a legal duty. This duty is independent of any contractual duty and is imposed by law, although it can be related to, or arise out of, the contractual duty.[77] Whether a breach of the duty constitutes a tort, however, requires a judicial balancing of three factors: (1) the special relationship between the parties, (2) the reasonable foreseeability of harm to the person injured, and (3) public policy concerns.[78]

Applying this test to insurance contracts, the court in *Hickman* stated that Indiana has long recognized an implied legal duty in all insurance contracts that the insurer will deal in good faith.[79] There is a special relationship between insurer and insured, at times an arms length dealing between the parties, but sometimes a fiduciary relationship and at other times an adversarial one.[80] Harm to the insured is easily foreseeable when a valid claim is denied in bad faith, and public policy demands fair play between the parties.[81] Although the court did not determine the precise extent of the insurer's legal duty, it did state that the duty is breached when the insurer makes an "unfounded" refusal to pay policy proceeds, causes an "unfounded" delay in making payment, "deceives" the insured, or exercises any "unfair advantage" to pressure an insured into a settlement of his claim.[82]

The tort is not committed every time an insurance claim is erroneously denied, of course. An insurer may dispute liability or the amount of recovery in good faith, and the mere lack of diligent investigation of the claim is not enough to justify punitive damages. Moreover, even if the tort is committed, it does not give rise to punitive damages unless there is "clear and convincing evidence that the defendant acted with malice, fraud, gross negligence, or oppressiveness which was not the result of a mistake of fact or law, honest error of judgment, overzealousness, mere negligence, or other human failing."[83] Recent decisions reaffirm this heightened burden of proof. In *Creative Demos*, for instance, a jury award of punitive damages was overturned even though a Sam's Club

76. 622 N.E.2d 515 (Ind. 1993).

77. *See id.* at 518. The court quoted from an early Twentieth Century case, *Peru Heating Co. v. Lenhart*, 95 N.E. 680 (Ind. App. 1911) ("[A] tort is one's disturbance of another in rights which the law has created, either in the absence of contract or in consequence of a relation which a contract has established between the parties.") *Id.*

78. *See Hickman*, 622 N.E.2d at 518.

79. *Id.*

80. *See id.*

81. *See id.*

82. *Id.* at 518-19.

83. Budget Car Sales v. Scott, 662 N.E.2d 638, 639 (Ind. 1996).

representative lied to the plaintiffs to obtain important proprietary information about running their business.[84]

These decisions make it more difficult to recover punitive damages in contract actions. Proving the elements of an established tort will usually be more difficult than showing that the defendant breached a contract with malice or oppression. There are traditional tort theories to consider, however, in many contract actions. Fraud or deceit might be proved when the breaching party has acted dishonestly while breaching the agreement. The plaintiff may be able to prove that the defendant entered into the contract not intending to perform, or misled the plaintiff into thinking she would perform, knowing that the contract would likely be breached. To prove the tort, the plaintiff will have to establish false or misleading statements, the defendant's knowledge of falsity, intent that the plaintiff rely on the misrepresentations, actual reliance, and resulting injury.[85] The tort of conversion might also be alleged when the defendant has not only breached, but unlawfully retained the plaintiff's property in doing so.[86]

An alternative is to seek expansion of tort law, as the plaintiff did in *Hickman.* It will be difficult to argue a tortious breach of an implied duty of good faith in all contracts because Indiana courts have steadfastly refused to recognize a general implied duty.[87] But other "special relationships," in addition to insurance, have been recognized as candidates for punitive damages in other jurisdictions over the years. Although the law in this area is changing rapidly, successful tort actions have usually involved plaintiffs with little or no bargaining power who are in a particularly vulnerable position if the defendant takes an unreasonably firm position. Claims in the past two decades have involved exploitation of an employment relationship,[88] breach of fiduciary duty (trusts and banking applications),[89] bad faith denial of the existence of a contract,[90]

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84. Creative Demos, Inc. v. Wal-Mart Stores, Inc., 142 F.3d 367, 370 (7th Cir. 1998). *See also* Colley v. Indiana Farmers Mut. Ins. Co., 691 N.E.2d 1259, 1261 (Ind. Ct. App. 1998).

85. *See In re* Gerard, 634 N.E.2d 51 (Ind. 1994). In fact, in one of the most celebrated punitive damages contract cases, the Indiana Supreme Court stated that the elements of fraud were arguably present in a breach of warranty action against an automobile dealer. *See* Hibschman Pontiac, Inc. v. Batchelor, 362 N.E.2d 845 (Ind. 1977).

86. *See* Chaiken v. Eldon Emmor & Co., 597 N.E.2d 337, 345 (Ind. Ct. App. 1992) (holding that conversion is the knowing exertion of unauthorized control over the property of another).

87. *See* First Fed. Sav. Bank of Ind. v. Key Markets, Inc., 559 N.E.2d 600 (Ind. 1990).

88. *See* Monge v. Superior Court, 176 Cal. App. 3d 503 (1986). *But see* Tacket v. General Motors Corp., 818 F. Supp. 1243 (S.D. Ind. 1993) (refusing to allow punitive damages in employment contract).

89. *See* G & N Aircraft, Inc. v. Boehm, 703 N.E.2d 665 (Ind. Ct. App. 1998) (involving minority shareholder of closely held corporation against majority shareholder and corporation); *see also* Wagman v. Lee, 457 A.2d 401 (D.C. 1983).

90. *See* Seaman's Direct Buying Serv. v. Standard Oil of Cal., 686 P.2d 1158 (Cal. 1984). The recent trend, however, is to retreat from the tort of bad faith breach of contract. In California (where the tort had expanded for years), the supreme court has now overruled *Seamans* and other leading decisions, limiting the tort to insurance relationships. *See* Freeman & Mills, Inc. v.

retaliatory refusal to pay back wages,[91] bad faith failure to expeditiously perform a contract,[92] willful and wanton breach of a loan commitment,[93] and a landlord's failure to honor commitments with reckless disregard of the tenant's rights.[94]

The Indiana Supreme Court is not likely to expand traditional tort law to accommodate more claims for punitive damages arising out of contractual relationships. *Best Beers* was an attempt to restrict punitive damages claims, and courts will be reluctant to move in the other direction. The test set out in the *Hickman* case, however, is worded generally enough that lawyers may in good faith allege tortious conduct in many cases where a "special" contractual relationship exists.

IV. Attorney's Fees

Indiana follows the American Rule, which prohibits an award of attorney's fees against the losing party even though legal costs are a foreseeable consequence of breach.[95] Absent a contract provision, statutory authorization, or common law exception, each party must pay his or her own attorney.[96] There are dozens of attorney's fees provisions scattered throughout the Indiana Code, and the statutes should always be researched to see if any apply to the case. A sampling of provisions referencing fees that may be pertinent to contract litigation include: declaratory judgment actions,[97] marketing contracts with agricultural cooperatives,[98] repairs of audio entertainment products,[99] bad checks,[100] confession of judgments in bills and notes,[101] trademark or trade name

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Southwest Forest Indus., Inc., 900 P.2d 669 (Cal. 1995). *See generally* James Nehf, *Bad Faith Breach of Contract in Consumer Transactions, in* Good Faith in Contract—Context and Concept 115 (Roger Brownsword et al. eds., 1999).

91. *See* Caplan v. St. Joseph's Hosp., 188 Cal. App. 3d 1193 (1987).

92. *See* Jardine, Stephenson, Blewett & Weaver v. United States Fidelity & Guar. Co., 91 F.R.D. 284 (D. Mont. 1981).

93. *See* Podleski v. Mortgage Fin., Inc., 709 P.2d 18 (Colo. Ct. App. 1985), *rev'd*, 742 P.2d 900 (Colo. 1987).

94. *See* Hilder v. St. Peter, 478 A.2d 202 (Vt. 1984).

95. *See* Salcedo v. Toepp, 696 N.E.2d 426 (Ind. Ct. App. 1998); Barrington Mgmt. Co. v. Paul E. Draper Family Ltd. Partnership, 695 N.E.2d 135 (Ind. Ct. App. 1998); Indiana Glass Co. v. Indiana Mich. Power Co., 692 N.E.2d 886, 889 & n.3 (Ind. Ct. App. 1998) (noting that attorney's fees not compensable as consequential damages under UCC § 2-715; also noting, however, that fees may be recoverable when incurred by a buyer in third-party litigation, e.g., in defense of personal injury action brought by third-party consumer).

96. *See* Dotlich v. Dotlich, 475 N.E.2d 331 (Ind. Ct. App. 1985).

97. Ind. Code §§ 34-14-1-10, -52-1-1 (1998).

98. *Id.* §§ 15-7-1-24, -26.

99. *Id.* §§ 26-2-6-4, -7.

100. *Id.* § 34-24-3-1.

101. *Id.* § 34-54-3-1.

actions,[102] continuing care contracts,[103] home improvement contracts,[104] breach of warranty in home construction,[105] conversion of property,[106] failure to pay employee wages,[107] distress sales,[108] lost or destroyed documents of title,[109] environmental marketing claims,[110] franchises,[111] conveyance of hazardous substances,[112] landlord and tenant security deposits,[113] lemon law,[114] mechanics liens,[115] unfair practices by motor vehicle dealers,[116] rental-purchase agreements,[117] deceptive consumer sales,[118] securities violations,[119] storage liens,[120] telephone solicitation contracts,[121] and termination of wholesale sales representative contracts.[122] The statutes must be read carefully, however, because they are often narrowly drafted, and some contain conditions or limitations.

Indiana courts recognize three general common law exceptions to the American Rule as well:

(1) Obdurate behavior: Courts use their equitable power to impose costs on defendants who behave in bad faith.

(2) Common funds: Courts use their equitable power to ensure that the beneficiaries of litigation are the ones who share the expense. This prevents the unjust enrichment of "free riders."

(3) Private attorney generals: Courts use their equitable power to insure the effectuation of a strong public policy.[123]

The obdurate behavior exception is the one most likely to be useful in a breach of contract action. Its parameters are codified in Indiana Code section 34-52-1-1, which authorizes an award of attorney's fees in any civil action as part

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102. *Id.* § 24-4-5-7.
103. *Id.* § 23-2-4-20.
104. *Id.* § 24-5-11.5-14.
105. *Id.* § 32-15-7-10.
106. *Id.* § 34-24-3-1.
107. *Id.* § 22-2-4-4.
108. *Id.* § 25-18-1-21.
109. *Id.* § 26-1-7-601.
110. *Id.* § 24-5-17-14.
111. *Id.* § 23-2-2.5-28.
112. *Id.* § 13-25-3-15.
113. *Id.* § 32-7-5-12.
114. *Id.* § 24-5-13-22.
115. *Id.* § 32-8-1-2.
116. *Id.* § 9-23-6-9.
117. *Id.* § 24-7-9-4.
118. *Id.* § 24-5-0.5-4.
119. *Id.* § 23-2-1-19.
120. *Id.* § 32-8-32-5.
121. *Id.* § 24-5-12-20.
122. *Id.* § 24-4-7-5.
123. *See* St. Joseph College v. Morrison, Inc., 302 N.E.2d 865 (Ind. App. 1973).

of costs to the prevailing party,[124] if the court finds that the party (1) brought an action or defense that is "frivolous, unreasonable or groundless;" (2) continued to litigate after the claim or defense "clearly became" frivolous, unreasonable or groundless; or (3) litigated the action in bad faith.[125] The trial court's decision to award fees will be reviewed under an abuse of discretion standard.[126]

In addition, Indiana Appellate Rule 15(G) provides that a court can award additional money, including attorney's fees, to the appellee if it affirms the award or judgment.[127] The award under this rule is discretionary and may be ordered when the appeal is "permeated with meritlessness, bad faith, frivolity, harassment, vexatiousness or purpose of delay."[128]

Courts tend to apply these exceptions more often in favor of defendants who have had to defend against a frivolous action brought by the plaintiff, but awards to plaintiffs have been made as well when the defendant stonewalls or has no legitimate defense.[129] While there is some overlap with Rule 11 of the Federal Rules of Civil Procedure, precedent under the federal rule is not determinative. Under Indiana law, a claim or defense is "frivolous" if

> (a) it is taken primarily for the purpose of harassing or maliciously injuring a person, (b) the lawyer is unable to make a good faith and rational argument on the merits of the action, or (c) the lawyer is unable to support the action taken by a good faith and rational argument for an extension, modification or reversal of existing law.[130]

"A claim or defense is groundless . . . if no facts exist that support the legal claim."[131] It is "unreasonable" if, "based on a totality of the circumstances, including the law and facts known at the time of the filing, no reasonable attorney would consider that the claim or defense was worthy of litigation or justified."[132] A finding of improper motive is not required.[133]

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124. The common law obdurate behavior exception and the statutory rule are not coextensive, however. Courts have held, for example, that the common law rule does not apply to obdurate behavior by defendants, but the statute does cover defendant conduct. *See* Mitchell v. Mitchell, 695 N.E.2d 920, 924 (Ind. Ct. App. 1998); *see also* IND. CODE § 34-52-1-1 (1998).

125. IND. CODE §§ 34-52-1-1(b)(1) to (3).

126. *See* Nelson v. Marchand, 691 N.E.2d 1264 (Ind. Ct. App. 1998).

127. *See* Young v. Butts, 685 N.E.2d 147, 151 (Ind. Ct. App. 1997); *see also* IND. R. APP. P. 15(G) (1998).

128. Orr v. Turco Mfg. Co., 512 N.E.2d 151 (Ind. 1987). *See generally* Donald Clementson-Mohr & Jeffrey A. Cooke, Comment, *Frivolous, Unreasonable or Groundless Litigation: What Shall the Standard Be for Awarding Attorney's Fees?*, 22 IND. L. REV. 299 (1989); Andrew W. Hull, Comment, *Attorney's Fees for Frivolous, Unreasonable or Groundless Litigation*, 20 IND. L. REV. 151 (1987).

129. The question whether attorney's fees should be awarded is to be decided by the court, not the jury. *See* O'Neill v. Goar, 622 N.E.2d 562 (Ind. Ct. App. 1993).

130. United Farm Bureau Mut. Ins. Co. v. Ira, 577 N.E.2d 588, 597 (Ind. Ct. App. 1991).

131. *Id.*

132. Kahn v. Cundiff, 533 N.E.2d 164, 170-71 (Ind. Ct. App.), *aff'd*, 543 N.E.2d 627 (Ind.

The obdurate behavior exception has some teeth. An example in a breach of contract case is *United Farm Mutual Insurance Co. v. Ira.*[134] Ira made a claim for medical benefits arising from a debilitating accident. To support his claim, Ira submitted the reports of two examining physicians who indicated that the injuries were caused by the accident. The company denied coverage, relying on a third report that raised questions about causation. When Ira ultimately prevailed, the trial court awarded attorney's fees, and the appellate court affirmed, finding that the insurance company's defense was not reasonable.[135] The third report was based upon a review of medical records only, and was made without examining Ira. Moreover, the report indicated that further investigation, including an examination, would be necessary to make a definitive finding. The company made no further effort to investigate the claim, choosing to deny coverage on the third report alone. The trial judge and court of appeals felt that this was too weak a basis for denying the claim and amounted to bad faith.[136]

A more predictable way to get the other party to pay attorney's fees, of course, is to provide for them in the contract. If the contract provides for attorney's fees, the provision will be enforced if it is not contrary to public policy.[137] This need not be a reciprocal obligation. A contract that only authorizes fees for one of the parties will be honored, though it will be reduced proportionately to the extent the opposing party prevails on a counterclaim.[138] Two recent cases illustrate, however, that recovery is by no means certain and fee provisions should be carefully drafted. *Salcedo v. Toepp*[139] involved the sale of a medical practice from Toepp to Salcedo. The transaction was embodied in several agreements, including an employment contract and lease. The documents each contained different language about attorney's fees. Toepp ultimately prevailed on an employment claim and successfully defended against Salcedo's claim under the lease. The trial court ruled that he was not entitled to attorney's fees under either contract.[140] The employment agreement only provided for fees to a prevailing party in an arbitration, and the parties chose not to arbitrate.[141] The lease provided that attorney's fees would be "added" to any judgment for a prevailing party, which the trial court interpreted to mean that there must first be a monetary recovery.[142] Because Toepp did not receive a money judgment in

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1989).

133. *See id.* at 171.

134. 577 N.E.2d 588 (Ind. Ct. App. 1991).

135. *Id.* at 597-98.

136. *Id.* at 595.

137. *See* Barrington Mgmt. Co. v. Paul E. Draper Family Ltd. Partnership, 695 N.E.2d 135, 142 (Ind. Ct. App. 1998).

138. *See* Willie's Constr. Co. v. Baker, 596 N.E.2d 958, 963-64 (Ind. Ct. App. 1992); Burras v. Canal Constr. & Design Co., 470 N.E.2d 1362 (Ind. Ct. App. 1984).

139. 696 N.E.2d 426 (Ind. Ct. App. 1998).

140. *See id.* at 436.

141. *See id.*

142. *See id.*

defending Salcedo's lease claim, the trial court could not "add" the fees to anything. The court of appeals affirmed on the employment contract but reversed under the lease, finding that the agreement should be interpreted as providing for fees to a prevailing party who successfully defends an action on the lease even without a monetary recovery.[143]

A more troubling case is *Barrington Management Co. v. Paul E. Draper Family Ltd. Partnership*.[144] The parties entered into a written agreement for the sale of commercial real estate. The agreement provided that attorney's fees were recoverable to a prevailing party "'in any legal or equitable proceeding against any other signatory brought under or with relation to the Contract or transaction . . . .'"[145] The seller brought an action seeking recission of the agreement when the buyer failed to fulfill certain conditions. At trial, the seller prevailed and the court granted recission plus attorney's fees.[146] On appeal, the fee award was set aside. The court observed that a party may either affirm a contract, retaining all its benefits and seek damages, or rescind the contract, return all the benefits received and reinstate the status quo.[147] The seller's choice of recission implied disaffirmance of the contract and all its contents, including the fee provision.[148] Because the plaintiff was suing for equitable recission and not for breach of the contract, it could not claim the benefits of the contract.

Barrington Management seems wrongly decided. It certainly frustrates the intent of the parties in drafting the provision. The contract itself contemplated a fee award in legal or equitable actions, which would include an action for recission. If the award cannot be made in an action to rescind the sale agreement, then the plaintiff is faced with either foregoing the equitable remedy or seeking fees. Indeed, if the court's view is correct, it would be impossible to get a fee award in any recission action, absent statutory authorization or a common law exception. The decision is particularly curious because the buyer had counterclaimed for specific performance,[149] so the seller clearly was a prevailing party in the buyer's equitable action.

V. PREJUDGMENT INTEREST

An award of prejudgment interest is often necessary to ensure that the prevailing party obtains the equivalent of full performance of the contract. If the defendant received goods but refused to pay the $10,000 price, awarding the plaintiff $10,000 three years later at trial is hardly the equivalent of having the

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143. *Id.*

144. 695 N.E.2d 135 (Ind. Ct. App. 1998).

145. *Id.* at 139 (quoting Purchase Agreement).

146. *See id.*

147. *Id.* at 142.

148. *See id.*

149. *See id.* at 135. The court apparently believed that the seller's action was unnecessary and that it would therefore be inequitable to award fees when the seller could have reached the same result without starting a lawsuit. *Id.* at 142-43.

use of $10,000 for the entire three-year period. The purpose of prejudgment interest is to compensate fully for the lost use of money during the pendency of litigation.[150]

The standard for determining when a court should award prejudgment interest is easy to state but difficult to apply. The award in a contract case is warranted if the terms of the contract made the claim readily ascertainable and the amount of the claim rests upon mere computation.[151] The award is proper where the trier of fact "need not exercise its judgment to assess the amount of damages."[152] Precedent indicates that the award is not a matter of discretion in state courts,[153] and the court of appeals has viewed it as a matter of right when the elements are satisfied.[154]

The justification for the standard is that the award should only be made where it is clear that the losing party owed a specific, liquidated amount of money at an identifiable date in the past. The classic example is a contract for the sale of goods where the buyer, without justification, fails to pay the contract price when due. The court can look at the contract and determine exactly how much was owed, and when it should have been paid.

In practice, however, Indiana courts have awarded prejudgment interest even when the terms of the contract did not make the amount of the claim readily ascertainable by mere computation. In *Sand Creek Country Club, Ltd. v. CSO Architects, Inc.*[155] an architectural firm sued Sand Creek Country Club for its fees earned in making drawings for the expansion of the clubhouse facilities. The contract (in the form of a letter agreement) did not specify the contract price for services to be rendered, but it did include a general fee arrangement. The firm performed substantial services and submitted a bill for $25,000, which the club did not pay. The firm subsequently sent another demand letter for $33,649, the asserted "value" of all services rendered. The firm ultimately prevailed at trial, and the judge awarded the $33,649 but no prejudgment interest.[156]

On appeal, the court upheld the damage award, but also found that the firm's demand letter made the damages "readily ascertainable" on the date it was delivered.[157] Prejudgment interest should therefore have been awarded from that

150. *See* Layden v. New Era Corp., 575 N.E.2d 638, 641 (Ind. Ct. App. 1990).

151. *See* Firstmark Standard Life Ins. v. Goss, 699 N.E.2d 689 (Ind. Ct. App. 1998); Hooker Builders, Inc. v. Smalley, 691 N.E.2d 1256 (Ind. Ct. App. 1998); Gershin v. Demming, 685 N.E.2d 1125 (Ind. Ct. App. 1997).

152. Sand Creek Country Club, Ltd. v. CSO Architects, Inc., 582 N.E.2d 872 (Ind. Ct. App. 1991); Monroe County Community Sch. v. Frohliger, 434 N.E.2d 93 (Ind. Ct. App. 1982).

153. *See Sand Creek Country Club*, 582 N.E.2d at 876.

154. *See, e.g.*, Dale Bland Trucking, Inc. v. Kiger, 598 N.E.2d 1103 (Ind. Ct. App. 1992); *cf.* DeLaCruz v. Pruitt, 590 F. Supp. 1296 (N.D. Ind. 1998) (noting that prejudgment interest is matter of discretion in federal court).

155. 582 N.E.2d 872 (Ind. Ct. App. 1991).

156. *See id.* at 874.

157. *Id.* at 876.

time.[158] In dissent, Judge Garrard viewed the standard more rigidly. Because the price was not specified in the contract, damages were the "reasonable value" of services rendered.[159] This was not a liquidated amount despite the fact that the architectural firm asserted a specific figure in its demand letter.[160] One of the practical lessons of this case is that there is good reason to draft a demand letter as specifically as possible, itemizing the amount allegedly owed, in hopes of convincing the court that damages were liquidated and easily ascertainable at that point.

The standard for awarding prejudgment interest was virtually ignored in *Jordan v. Talaga.*[161] The plaintiffs alleged that a developer breached the implied warranty of habitability in the construction of their home because of excessive water seepage problems. The appellate court held that the appropriate measure of damages was the difference between the value of the home as warranted and the value at the time of acceptance.[162] Even though these damages clearly were not liquidated or readily ascertainable at the time of breach (requiring a comparison of market values), the court stated that an award of prejudgment interest would be appropriate "because the deprivation of the appreciation of one's house is substantially similar to the deprivation of the use of money."[163]

Another lesson from the case law is that prejudgment interest will likely be awarded if the parties have stipulated to the damages prior to trial. This will make it much easier for the court to conclude that the damages were liquidated and ascertainable from the time of breach.[164] This may be an additional incentive to encourage the defendant to stipulate to a damage amount early in the litigation whenever damages are not at issue.[165]

VI. Liquidated Damages Provisions

One way of ensuring a specific amount of compensation for breach of contract is to stipulate the damages in the contract. Care must be taken in drafting the provision, however, for at least two reasons. First, a liquidated damages provision can be a hindrance to full recovery if it stipulates too low an amount. The clause can work either for or against the party seeking damages.

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158. *See id.*

159. *Id.* (Garrard, J., concurring in part and dissenting in part).

160. *See id.*

161. 532 N.E.2d 1174 (Ind. Ct. App. 1989).

162. *Id.* at 1187.

163. *Id.* (citing Fort Wayne Nat. Bank v. Scher, 419 N.E.2d 1308 (Ind. Ct. App. 1981)).

164. *See* Dale Bland Trucking, Inc. v. Kiger, 598 N.E.2d 1103 (Ind. Ct. App. 1992); *cf.* Hooker Builders, Inc. v. Smalley, 691 N.E.2d 1256 (Ind. Ct. App. 1998) (finding that contractor had nothing in the record indicating that damages were readily ascertainable; damages did become ascertainable after arbitration award, however).

165. Prejudgment interest has traditionally been simple interest. If a party wishes to receive compounded interest, the contract should so provide. *See* Firstmark Standard Life Ins. v. Goss, 699 N.E.2d 689, 694 (Ind. Ct. App. 1998).

An example is *Beck v. Mason*.[166] The Masons entered into a contract to purchase real estate from the Becks. The sale contract provided that if the Masons fail to purchase, the Becks would retain a $1000 earnest money deposit "as liquidated damages and not as a penalty or a forfeiture."[167] After the Masons backed out of the deal, the Becks tried to recover more than the $1000 because their actual damages were higher.

The court set out the rule in Indiana: A clause fixing damages in the contract does not per se restrict the remedies of the parties; where it appears that the parties so intended, the clause will be viewed as a minimum or alternative recovery, and the aggrieved party can sue for actual damages if they are greater.[168] On the intent issue, however, the court stated that by using the term "liquidated damages" the parties were demonstrating an intent to make the provision the exclusive remedy.[169] This construction "comports with the reasonable expectations of the contracting parties."[170] The court went on to hold, in rather expansive language, that unless the language is ambiguous, a liquidated damages provision will be presumed to be the sole remedy for breach.[171] A party should be able to avoid this result by stipulating that the damages are supplementary only, or by merely requiring that the deposit be "forfeited," without labeling the forfeiture a liquidated damages provision.

The second reason to draft a liquidated damages provision with care is to ensure that the court will not declare it an unenforceable penalty. The standard is not clearly enunciated in Indiana.[172] One formulation is that the provision is enforceable "where the nature of the contract is such that a breach would result in damages which are uncertain and difficult to prove, and the parties have fixed an amount that is not greatly disproportionate to the *loss likely to occur*."[173] This two-part inquiry looks at the reasonableness of the provision as a predictor of likely damages, in light of circumstances known to the parties at the time the contract was made.

A second statement of the rule, however, focuses on the reasonableness of the provision in light of the actual damages sustained after the breach. The court will ask two questions:

> (1) Does the liquidating provision attempt to secure an amount for the non-breaching party which is reasonably proportionate to the amount of *actual damages* which will be sustained in the event of breach? (2) Is the provision designed to represent the measure of *actual damages*, or is it

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166. 580 N.E.2d 290 (Ind. Ct. App. 1991).

167. *Id.* at 291.

168. *Id.* at 293 (citing Fletcher v. United States, 303 F. Supp. 583 (N.D. Ind. 1967)).

169. *Id.*

170. *Id.* at 294.

171. *Id.*

172. *See* Gershin v. Demming, 685 N.E.2d 1125, 1128 (Ind. Ct. App. 1997) ("no hard and fast guidelines to follow").

173. Harris v. Primus, 450 N.E.2d 80, 83 (Ind. Ct. App. 1983).

> an apparent effort to penalize the breaching party so that the damages will be disproportionate to the *actual damages* sustained?[174]

Most commentators and courts agree that the first formulation is the most appropriate.[175] The clause should be upheld if it is a reasonable effort at estimating probable damages at the time the contract was consummated, regardless of the actual harm that follows the breach. In practice, however, it seems virtually impossible for courts to ignore the actual consequences of the breach, and this factor almost always colors the court's judgment regardless of the standard it purports to use. A recent example is *Gershin v. Demming*,[176] where the court examined a lease providing for damages equal to one percent of monthly rent per day for each day the tenant's payment is past due. The court stated that the clause will be upheld if the stipulated sum is "not greatly disproportionate to the loss *likely to occur*."[177] It then struck down the provision because it yielded a sum "grossly disproportionate to Landlord's *actual loss*."[178]

Another illustration is *Woodbridge Place Apartments v. Washington Square Capital, Inc.*[179] A real estate developer contracted for a $4.6 million loan commitment from Washington Square Capital. The documents provided that if the developer did not go through with the loan, Washington would retain the developer's "standby deposit" of $139,950, which was 3% of the loan amount and standard in the industry.[180] The loan was never funded, and the developer sued for return of the deposit. Judge Brooks viewed the standby deposit as a liquidated damages provision, and not as consideration for an option contract, and declared it an unenforceable penalty.[181] He acknowledged that there were uncertainties involved in predicting damages when a borrower backs out of a loan transaction, but struck down the provision because Washington introduced no evidence that the 3% figure was designed to estimate actual losses.[182] The amount seemed "arbitrary" and not reasonably proportionate to the amount of

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174. Czeck v. Van Helsland, 241 N.E.2d 272, 274 (Ind. App. 1968).

175. *See, e.g.*, E. ALLEN FARNSWORTH, CONTRACTS 844-45 (3d ed. 1999). *Cf.* Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 225-36 (1995) (recommending a "second-look standard"). The UCC seems to sanction either approach, upholding the provision if the amount is "reasonable in light of the anticipated or actual harm caused by the breach." U.C.C. § 2-718(1). Regarding leases, UCC § 2A-504 speaks only of "anticipated harm." U.C.C. § 2A-504.

176. 685 N.E.2d 1125 (Ind. Ct. App. 1997).

177. *Id.* at 1127 (emphasis added).

178. *Id.* at 1129 (emphasis added). In another recent case, however, the federal district court did apply the "likely to occur" rule consistently. *See* Miami Valley Contractors, Inc. v. Town of Sunman, 960 F. Supp. 1366 (S.D. Ind. 1997).

179. No. EV87-204-C, 1991 WL 340619 (S.D. Ind. Jan. 10, 1991), *aff'd in part, rev'd in part*, 965 F.2d 1429 (7th Cir. 1992).

180. *See id.* at *3.

181. *Id.*

182. *Id.*

actual damages.[183] Significantly, Washington failed to offer evidence of any substantial actual losses, other than some administrative costs for processing the paperwork. Indeed, there may have been no actual injury because Washington subsequently loaned the money to a different borrower at a higher interest rate. One suspects that if the actual losses had been higher (i.e., interest rates had declined), the clause would have been upheld.

One of the most common places to find a liquidated damages provision is in a covenant not to compete. *Turbines, Inc. v. Thompson*,[184] discussed earlier,[185] illustrates the reason why: It can be difficult to prove lost profits resulting from an employee's breach of the covenant. Indiana courts have sent conflicting signals on their enforceability, however. In *Raymundo v. Hammond Clinic Ass'n*,[186] the Indiana Supreme Court upheld a clause that required an orthopedic surgeon to pay $25,000 if he breached a five-year commitment to work as a partner in a medical practice clinic. The contract included a covenant not to compete with the clinic following his departure. The court stated that it "will almost always uphold" a liquidated damages provision in a covenant not to compete unless the amount is "grossly disproportionate to the loss and far beyond any possible damages that could be incurred."[187] The court observed that it was altogether reasonable to assume that if Dr. Raymundo did not complete his five-year commitment, the clinic would incur the expense of finding a replacement as well as the loss of revenue.[188] In light of the fact that Dr. Raymundo was responsible for bringing in over $100,000 in revenue per year, the $25,000 damages provision was not excessive.[189]

In contrast, the court of appeals in *Hahn v. Drees, Perugini & Co.*,[190] struck down a liquidated damages provision in a contract between an accountant and an auditing firm. The agreement provided that if the employee terminated early and "perform[ed] any work in any manner for any fee whatsoever, for any client of the employer . . . [the employee must pay] three times the employers [sic] highest annual fee received from the client during the three most recent calendar years . . . ."[191] The court upheld the covenant in part, but held that the damages provision for breaching it was unenforceable.[192] It viewed the provision as an overbroad "shotgun clause" and therefore a penalty because it assessed treble damages regardless of whether the employee's contact with the firm's clients proved harmful in any way.[193] The contact might reduce the firm's income

183. *See id.*
184. 684 N.E.2d 254 (Ind. Ct. App. 1997).
185. *See supra* note 56 and accompanying text.
186. 449 N.E.2d 276 (Ind. 1983).
187. *Id.* at 277.
188. *Id.* at 284.
189. *See id.*
190. 581 N.E.2d 457 (Ind. Ct. App. 1991).
191. *Id.* at 459.
192. *Id.* at 463.
193. *Id.*

greatly or hardly at all. The provision thus had no relationship to the injury the firm would likely suffer. Strictly speaking, the treble damages provision was not, in the language of *Raymundo*, "far beyond any possible damages that could be incurred." Taking a large auditing client away from the firm might cause a substantial loss of profits for many years. Nevertheless, the provision would seem to impose excessive damages in most instances, and there was no evidence of substantial actual injury. Besides, "treble" damages sounds punitive and more like a penalty for contract breach.

These last two cases illustrate the limits of liquidated damages clauses in employment contracts. When drafting such provisions, the lawyer should always ask whether he or she is legitimately trying to estimate actual losses or is merely creating a disincentive for the employee to terminate the contract. To increase the probability of enforcement, the clause should be drafted with language that shows a genuine attempt to predict future injury, recognizing the uncertainties in predicting what those injuries might be. Language suggesting a penalty for nonperformance should be avoided.[194]

CONCLUSION

Indiana case law is not unfriendly to plaintiffs in contract actions. Courts tend to give parties a great deal of freedom in drafting contract terms,[195] which can assist nonbreaching parties who planned ahead and then bring an action to enforce damage-enhancing provisions on the subject of liquidated damages and attorney's fees. Courts are not particularly strict in applying the standard for awarding prejudgment interest, granting the award even in cases where the damages were not "readily ascertainable" at an earlier date. Nor are they hostile to claims for consequential damages, including lost profits, so long as there is reasonably reliable, objective evidence to sustain them. While the current rules preclude punitive damages in contract actions, the *Hickman* standard for recognizing tortious conduct allows room for expansion in this area as well. In sum, Indiana remains a state in which good lawyering, from the contract drafting stage through litigation, can increase the chances of realizing full compensation, or at least something close to that amount, for a breach of contract.

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194. Using "penalty" language will not be decisive, however. In *Miami Valley Contractors, Inc. v. Town of Sunman*, 960 F. Supp. 1366 (S.D. Ind. 1997), the district court upheld a liquidated damages clause even though it provided that "a penalty shall be paid by the Contractor to the Owner" for late completion of the project. *Id.* at 1377.

195. *See, e.g.*, Trimble v. Ameritech Publ'g, Inc., 700 N.E.2d 1128, 1129 (Ind. 1998) ("Courts in Indiana have long recognized the freedom of parties to enter into contracts and have presumed that contracts represent the freely bargained agreement . . . . We continue to believe that 'it is in the best interest of the public not to restrict unnecessarily persons' freedom of contract.'") (citations omitted).

RECENT DEVELOPMENTS IN INDIANA CRIMINAL LAW AND PROCEDURE

JOEL M. SCHUMM*

This Article surveys developments in the area of criminal law and procedure that were enacted by the 1998 General Assembly and addressed by the Indiana appellate courts since the last survey period.

I. 1998 LEGISLATIVE ENACTMENTS

In its forty-seven day[1] short session, the 110th General Assembly enacted several bills that impact the criminal statutes in relatively minor ways. The Indiana General Assembly overrode Governor Frank O'Bannon's veto of an act that amended several criminal statutes to provide liability for conduct that results in the death of a viable fetus.[2] These changes specifically except legally performed abortions.[3] The definition of "serious bodily injury" now includes bodily injury that creates a substantial risk of death or that causes "loss of a fetus."[4] The murder,[5] voluntary manslaughter,[6] and involuntary manslaughter[7] statutes were amended to criminalize the killing of a fetus. The aggravated battery statute now imposes liability for the "loss of a fetus."[8] A fetus is defined as a "fetus that has attained viability (as defined in [Indiana Code section] 16-18-2-365)."[9] Finally, the death penalty statute was also amended to add as an aggravating circumstance (permitting the State to seek either a death sentence or a sentence of life imprisonment without parole) that "[t]he victim of the murder was pregnant and the murder resulted in the intentional killing of a fetus that has attained viability."[10]

The legislature also created the new criminal offense of money laundering, which is generally a Class D felony but becomes a Class C felony if the value of the proceeds or funds is at least $50,000.[11] The crime is committed by:

> A person who knowingly or intentionally: (1) acquires or maintains an

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* B.A., 1992, Ohio Wesleyan University; M.A., 1994, University of Cincinnati; J.D., 1998, Indiana University School of Law—Indianapolis.

1. *See* Suzanne McBride, *Lawmakers Got Paid $2.6 Million. Each Got At Least $17,800 During the Past Session, While some of the Biggest Issues Went Unresolved*, INDIANAPOLIS STAR, Apr. 26, 1998, at B1.
2. P.L. No. 261-1997, 1998 Ind. Acts 1 (vetoed by governor, May 12, 1997; passed over veto, Jan. 22, 1998).
3. IND. CODE § 35-42-1-0.5 (1998).
4. *Id.* § 35-41-1-25(5).
5. *Id.* § 35-42-1-1(4).
6. *Id.* § 35-42-1-3(a)(2).
7. *Id.* § 35-42-1-4(c).
8. *Id.* § 35-42-2-1.5(3).
9. *See, e.g.*, *id.* § 35-42-1-1(4).
10. *Id.* § 35-50-2-9(b)(16).
11. *See id.* § 35-45-15-5.

> interest in, receives, conceals, possesses, transfers, or transports the proceeds of criminal activity; (2) conducts, supervises, or facilitates a transaction involving the proceeds or criminal activity; or (3) invests, expends, receives, or offers to invest, expend, or receive, the proceeds of criminal activity or funds that are the proceeds of criminal activity, and the person knows that the proceeds or funds are the result of criminal activity.[12]

The statute also provides that it is a defense to the crime if the person acted with intent to facilitate a lawful seizure or forfeiture,[13] if the transaction was necessary to preserve a person's right to counsel,[14] or if the funds were received as legal fees, provided the attorney did not have actual knowledge that the funds were derived from criminal activity.[15]

The definition of lawful detention was amended to include "placement in a community corrections program's residential facility or electronic monitoring."[16] Now, a "person who knowingly or intentionally violates a home detention order and intentionally removes an electronic monitoring device commits escape, a Class D felony."[17]

Cruelty to an animal[18] remains a Class A misdemeanor in most cases, however, the statutory definition was changed, some exceptions were added, and whenever the offender has a prior unrelated conviction for the same offense it may now be charged as a Class D felony.[19] Previously, the crime was defined as a person who knowingly or intentionally (1) tortures, beats, or mutilates a vertebrate animal resulting in serious injury or death to the animal; or (2) kills a vertebrate animal without the authority of the owner of the animal.[20] The amended statute now criminalizes the conduct whenever a person "tortures, beats, or mutilates a vertebrate animal" but provides an exception if the person was "engaged in a reasonable and recognized act of training, handling, or disciplining the vertebrate animal."[21]

The resisting law enforcement statute was amended to make the offense a Class D felony if a person flees from a law enforcement officer with the use of a vehicle.[22] The offense remains a Class A misdemeanor in most other circumstances.[23]

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12. *Id.*
13. *Id.* § 35-45-15-5(b).
14. *Id.* § 35-45-15-5(c)(1).
15. *Id.* § 35-45-15-5(c)(2).
16. *Id.* § 35-41-1-18(a)(7).
17. *Id.* § 35-44-3-5(b).
18. *Id.* § 35-46-3-12.
19. *Id.* § 35-46-3-12(a).
20. *Id.* § 35-46-3-12(a) (1993) (amended by *id.* § 35-46-3-12(a)(1998)).
21. *Id.* §§ 35-46-3-12(a) & (b)(2) (1998).
22. *Id.* § 35-44-3-3(b)(1)(A).
23. *Id.* § 35-44-3-3(a).

The general assembly also amended several statutes to provide enhanced charges for the crimes of rape,[24] criminal deviate conduct,[25] child molesting,[26] vicarious sexual gratification,[27] sexual battery,[28] and sexual misconduct with a minor[29] when

> the commission of the offense is facilitated by furnishing the victim, without the victim's knowledge, with a drug (as defined in [Indiana Code section] 16-42-19-2(1)) or a controlled substance (as defined in [Indiana Code section] 35-48-1-9) or knowing that the victim was furnished with the drug or controlled substance without the victim's knowledge.[30]

The legislature also established as a new statutory aggravating circumstance, which trial courts may consider when imposing sentence, that

> [b]efore the commission of the crime, the person administered to the victim of the crime, without the victim's knowledge, a sedating drug or a drug that had a hypnotic effect on the victim, or the person had knowledge that such a drug had been administered to the victim without the victim's knowledge.[31]

The legislature also added another statutory aggravating circumstance that "the injury to or death of the victim of the crime was the result of shaken baby syndrome (as defined in [Indiana Code section] 16-41-40-2)."[32]

The bail statute was amended and now allows trial courts to increase bail if the state presents additional "clear and convincing evidence: (A) of the factors described in [Indiana Code section] 33-14-10-6(1)(A)[33] and [Indiana Code section] 33-14-10-6(1)(B);[34] or (B) that the defendant otherwise poses a risk to the physical safety of another person or the community."[35] The statute previously provided for an increase in bail only when the state presented additional "evidence relevant to a high risk of nonappearance, based on the factors set forth in section 4(b) of this chapter."[36] This change follows a 1996 amendment that

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24. *Id.* § 35-42-4-1(b)(4).
25. *Id.* § 35-42-4-2(b)(4).
26. *Id.* §§ 35-42-4-3(a)(4) & (b)(3).
27. *Id.* §§ 35-42-4-5(a)(2)(B) & (b)(3).
28. *Id.* § 35-42-4-8(b)(3).
29. *Id.* §§ 35-42-4-9(a)(2) & (b)(2).
30. *Id.* §§ 35-42-4-1(b)(4), -2(b)(4), -3(a)(4), -3(b)(3), -5(a)(2)(B), -5(b)(3), -8(b)(3), -9(a)(2), -9(b)(2).
31. *Id.* § 35-38-1-7.1(b)(12).
32. *Id.* § 35-38-1-7.1(b)(11).
33. "[T]hat an act or threat of physical violence or intimidation has been made against the victim or the immediate family of the victim." *Id.* § 33-14-10-6(1)(A).
34. "[T]hat the act or threat has been made by the defendant and the direction of the defendant." *Id.* § 33-14-10-6(1)(B).
35. *Id.* § 35-33-8-5(b)(2).
36. *Id.* § 35-33-8-5 (1993) (amended by *id.* § 35-33-8-5 (1998)).

allowed courts to consider whether a "defendant poses a risk of physical danger to another person or the community" and consider factors "to assure the public's physical safety" when setting bail.[37] The amended statute further provides that the court may not reduce bail "if [it] finds by clear and convincing evidence that the factors described in [Indiana Code section] 33-14-10-6(1)(A)[38] and [Indiana Code section] 33-14-10-6(1)(B)[39] exist or that the defendant otherwise poses a risk to the physical safety of another person or the community."[40]

Finally, the general assembly also enacted a statute that now allows counties to require individuals (1) sentenced to a county jail for a felony or misdemeanor, (2) subject to lawful detention in a county jail for more than seventy-two hours, (3) not a member of a family that makes less than 150% of the federal income poverty level, and (4) not detained as a child subject to juvenile court jurisdiction, to reimburse the county for the cost of incarceration.[41] At the time of sentencing the trial court "shall affix" the amount of this reimbursement that (1) may not exceed an amount the person can or will be able to pay, (2) does not harm the person's ability to reasonably be self-supporting or to reasonably support any dependent(s), and (3) takes into consideration and gives priority to any other restitution, reparation, repayment, cost, fine, or child support obligations that the defendant is required to pay.[42]

II. Case Developments

A. Search and Seizure

In *Jaggers v. State*, the supreme court granted transfer "to address the interplay between the 'good faith' exception to the exclusionary rule and the warrant statute, Indiana Code [section] 35-33-5-2."[43] In that case, an Indiana state trooper received an anonymous call asserting that Jaggers was growing and trafficking marijuana in his house. The caller claimed that (1) he had personally seen marijuana in and around Jaggers home on numerous occasions and (2) Jaggers was growing marijuana on two separate plots of land a few miles from Jaggers' house. The officer visited both plots of land, which were easily accessible to the public, and found marijuana growing there. Based on the officer's testimony at a probable cause hearing, a magistrate issued a warrant authorizing a search of Jaggers' home.[44] The search uncovered a substantial

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37. *Id.* § 35-33-8-3.1(a) (1993 & Supp. 1996) (recodified and amended by *id.* § 35-33-8-5 (1998)). *See also* Gary L. Miller & Joel M. Schumm, *Recent Developments in Indiana Criminal Law and Procedure*, 30 IND. L. REV. 1005, 1005 (1997).

38. *See supra* note 32.

39. *See supra* note 33.

40. IND. CODE § 35-33-8-5(c) (1998).

41. *Id.* § 36-2-13-15(c).

42. *Id.* § 35-50-5-4(c).

43. 687 N.E.2d 180, 181 (Ind. 1997).

44. *See id.*

amount of marijuana and related paraphernalia, which Jaggers unsuccessfully moved to suppress before trial.[45]

Quoting *Illinois v. Gates*,[46] the supreme court noted that "'[i]nformants' tips doubtless come in many shapes and sizes from many different types of persons. . . . Rigid legal rules are ill-suited to an area of such diversity.'"[47] In *Jaggers*, however, the "search warrant . . . was issued on uncorroborated hearsay from an informant whose credibility was entirely unknown. This does not satisfy the Fourth Amendment's requirement of probable cause."[48] In addition, the court found that the hearsay in the case failed to satisfy Indiana's statute regulating the issuance of search warrants based on hearsay.[49]

As a final point, the court considered whether the evidence was nevertheless admissible under *United States v. Leon*,[50] which holds that "the exclusionary rule does not require the suppression of evidence obtained in reliance on a defective search warrant if the police relied on the warrant in objective good faith."[51] The good faith exception does not apply, however, if "the warrant was based on an affidavit 'so lacking in indica of probable cause as to render official belief in its existence entirely unreasonable.'"[52] The court observed that the uncorroborated hearsay "on which the warrant was based was so lacking in indicia of probable cause that no well-trained officer would reasonably have relied on the warrant."[53] Noting that *Leon*'s rationale would not be advanced "by effectively allowing the State to claim good faith reliance on a warrant after a less than faithful effort to establish probable cause to obtain it," the court held that the good faith exception did not save the illegally-seized evidence at issue in *Jaggers*.[54]

In *Perkins v. State*,[55] the court of appeals considered the validity of a search incident to lawful arrest. During the execution of a search warrant at a residence, police officers believed that Perkins, who was standing on the porch, was "either reaching for something or concealing something [and o]rdered him to lie down two or three times."[56] He did not comply and the officers pushed him to the floor, handcuffed him, and then entered the house.[57] Perkins first argued that the police were not justified in conducting a limited frisk of his person pursuant to *Terry v. Ohio*.[58] The court rejected this argument and held that "Perkins' actions

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45. *See id.* at 181-82.
46. 462 U.S. 213 (1983).
47. *Jaggers*, 687 N.E.2d at 182 (quoting *Gates*, 462 U.S. at 232).
48. *Id.* at 183.
49. *Id.* at 183-84; *see also* IND. CODE § 35-33-5-2 (1998).
50. 468 U.S. 897 (1984).
51. *Jaggers*, 687 N.E.2d at 184.
52. *Id.* (quoting *Leon*, 468 U.S. at 923).
53. *Id.* at 185.
54. *Id.* at 186.
55. 695 N.E.2d 612 (Ind. Ct. App. 1998).
56. *Id.* at 613.
57. *See id.*
58. 392 U.S. 1 (1968) (holding that a police officer may make a reasonable search for

on the porch were sufficient to justify the officers' concerns for their safety and the *Terry* frisk."[59]

The police discovered a handgun during that frisk, and discovered marijuana during a subsequent search. Perkins sought to suppress the marijuana on the basis that the officer did not have probable cause to arrest him for carrying a handgun without a license at the time of the marijuana's discovery.[60] Individuals may legally carry an unlicenced handgun on their own property, and Perkins was at a residence when the handgun was discovered.[61] Because the State has the burden to justify a warrantless search and the record was not clear whether the search took place before or after Perkins provided information justifying his arrest for carrying a handgun without a license, the court of appeals reversed the trial court's denial of the motion to suppress the marijuana.[62]

In *Carter v. State*,[63] a police officer in plain clothes observed the defendant standing in line at a restaurant. The officer recognized Carter as a person with a prior cocaine conviction and saw Carter "turn toward his direction as the crowd of people entered the restaurant and then turn back toward the counter," place his right hand in his coat pocket, then turn and walk with "long steps" toward the door, bumping into the officer's partner as he exited.[64] The officer followed Carter outside and, as Carter approached a car, the officer reached around and patted the right pocket of Carter's coat. The officer felt what he believed to be a gun, pulled Carter's hand from the coat pocket, retrieved the gun, and placed Carter under arrest.[65]

Carter filed a motion to suppress the evidence obtained during this warrantless search, and the motion was denied by the trial court.[66] Upon consideration of the "totality of the circumstances," the court of appeals reversed the trial court, holding that "the facts and the reasonable inferences arising from the facts would not cause an ordinarily prudent person to believe that criminal activity had or was about to occur."[67]

In *Haley v. State*,[68] the court of appeals considered "[w]hether a person camping in a tent erected in a public campground is entitled to constitutional protection against unreasonable search and seizure[,] an issue of first impression

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weapons on a person the officer believes to be armed and dangerous, if the officer reasonably believes that the officer's safety or the safety of others is endangered).

59. *Perkins*, 695 N.E.2d at 614.

60. *See id.*

61. *See id.*; *see also* IND. CODE § 35-47-2-1 (1998).

62. *Perkins*, 695 N.E.2d at 614.

63. 692 N.E.2d 464 (Ind. Ct. App. 1997).

64. *Id.* at 465.

65. *See id.*

66. *See id.*

67. *Id.* at 467-68.

68. 696 N.E.2d 98 (Ind. Ct. App.), *trans. denied*, No. 66A03-9706-CR-223 (Ind. Oct. 28, 1998).

in Indiana.'"[69] The court noted that Indiana cases have held that a person renting a hotel or motel room may have a legitimate expectation of privacy in the room.[70] The court agreed with the defendant "that the constitutional protections provided to those who rent hotel rooms should also extend to those who choose to make their 'transitory home' a tent, if they have exhibited a subjective and reasonable expectation of privacy in that tent."[71] The court ultimately concluded that the warrantless seizure of the contraband inside the tent was not justified by exigent circumstances, because it is not likely that the marijuana cigarette at issue would have been "so totally consumed that no evidence of its existence remained."[72]

In *L.A.F. v. State*,[73] the court of appeals addressed whether officers patrolling a housing complex at 12:30 a.m. were justified in performing a *Terry* frisk of a juvenile sleeping in the back seat of a car that they stopped. The court held that the search violated the Fourth Amendment.[74]

> The fact that the officers were investigating L.A.F. and another individual for curfew violations and that L.A.F. had been sleeping in a car at the time the officers arrived is insufficient for a reasonably prudent man to be warranted in the belief that his safety or that of others was in danger.[75]

The trial court erred by admitting into evidence the handgun found during the search.[76]

A similar issue was presented in *State v. Joe*.[77] In that case, the court of appeals considered whether police officers were justified in conducting a *Terry* search for weapons of a car pulled over for speeding and driving left of center. The police were patrolling a neighborhood well known for drug trafficking and shootings. After stopping the car, the driver (Joe) began fidgeting with his hand between the console and the driver's seat, and the police ordered him to put his hands where they could be seen.[78] He did not comply until after the police officer made repeated demands and had drawn his gun. Based on these circumstances, the court upheld the search, noting that "Joe's actions gave rise to a reasonable belief that a limited search of the interior of the car for weapons was necessary to ensure the officers' safety."[79]

In *Parker v. State*,[80] the court of appeals addressed the "plain feel" seizure

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69. *Id.* at 100-01.
70. *Id.* at 101.
71. *Id.*
72. *Id.* at 103.
73. 698 N.E.2d 355 (Ind. Ct. App. 1998).
74. *Id.* at 356.
75. *Id.*
76. *See id.*
77. 693 N.E.2d 573 (Ind. Ct. App. 1998).
78. *See id.* at 574.
79. *Id.* at 575.
80. 697 N.E.2d 1265 (Ind. Ct. App. 1998).

of cocaine found in a suspect's front pants pocket during a patdown search for weapons. The plain feel doctrine was first recognized by the U.S. Supreme Court in *Minnesota v. Dickerson*:

> If a police officer lawfully pats down a suspect's outer clothing and feels an object whose contour or mass makes its identity immediately apparent, there has been no invasion of the suspect's privacy beyond that already authorized by the officer's search for weapons; if the object is contraband, its warrantless seizure would be justified by the same practical considerations that inhere in the plain view context.[81]

The officer who performed the patdown search testified at trial that he "merely suspected" that the object was narcotics.[82] Because the identity of the object must be "immediately apparent or instantaneously ascertainable," the plain feel doctrine was not satisfied and the seizure violated the Fourth Amendment.[83]

The plain feel doctrine was also considered in *Burkett v. State*.[84] After pulling over Burkett's car for speeding, the police officer smelled alcohol on the defendant's breath, asked him to take some field sobriety tests, and ultimately administered a portable breath test that registered a blood alcohol content of .08.[85] The officer then escorted Burkett to his police car to transport him to the county jail for a certified breath test. While conducting a patdown search prior to placing Burkett in the police car, the officer felt a round, hard object that he immediately recognized from his experience to be a "one hitter," a pipe used to smoke marijuana.[86] Upon removal of the object from Burkett's pocket, the officer found that it was not a pipe but was a green leafy substance tightly rolled in a plastic bag.[87] The substance tested positive for marijuana. Burkett was charged with possession of marijuana and moved to suppress the evidence, contending that the officer had no basis for conducting a patdown search.[88] Because the police officer would be alone with Burkett in his vehicle as he transported him to the county jail, "a reasonably prudent man in the same circumstances would be warranted to pat down Burkett for his own safety."[89] Accordingly, the trial court properly denied Burkett's motion to suppress.[90]

B. Confessions

The supreme court considered the admissibility of a defendant's

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81. 508 U.S. 366, 375-76 (1993).
82. *See Parker*, 697 N.E.2d at 1268.
83. *Id.*
84. 691 N.E.2d 1241 (Ind. Ct. App. 1998), *trans. denied*, 698 N.E.2d 1194 (Ind. 1998).
85. *See id.* at 1243.
86. *See id.*
87. *See id.*
88. *See id.* at 1243-44.
89. *Id.* at 1244.
90. *See id.* at 1245.

incriminating statement to police in a few different contexts. In *Taylor v. State*,[91] the supreme court considered whether a defendant's *Miranda* rights[92] were violated when police continued to question him after he said: "I don't know what to say. I guess I really want a lawyer, but, I mean, I've never done this before so I don't know."[93] The supreme court applied the standard set forth by the U.S. Supreme Court in *Davis v. United States*.[94] "Invocation of the *Miranda* right to counsel requires, at a minimum, some statement that can reasonably be construed to be an expression of a desire for the assistance of an attorney."[95] The level of clarity required is whether a "reasonable police officer in the circumstances would understand the statement to be a request for an attorney."[96] Davis's statement that "maybe I should talk to a lawyer" was held not to be a request for counsel.[97] The holding of *Davis*, as summarized in *Taylor*, is that "police have no duty to cease questioning when an equivocal request for counsel is made. Nor are they required to ask clarifying questions to determine whether the suspect actually wants a lawyer."[98] The four member majority[99] of the court concluded that Taylor's comments were nothing more than "think[ing] out loud," an expression of doubt and not an unambiguous request for a lawyer.[100] Accordingly, Taylor's statement to the police following this ambiguous request was properly admitted into evidence.[101]

In *Sauerheber v. State*,[102] the court considered the significance of the timing of a defendant's request for counsel. Sauerheber made several requests for an attorney in the presence of a detective during the execution of a search warrant for the collection of samples of his hair, saliva, and blood.[103] Four days later, the police interrogated him after securing a *Miranda* waiver. Sauerheber argued that his confession should have been suppressed based on *Edwards v. Arizona*,[104]

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91. 689 N.E.2d 699 (Ind. 1997).
92. Miranda v. Arizona, 384 U.S. 436 (1966).
93. *Taylor*, 689 N.E.2d at 702-03.
94. 512 U.S. 452 (1994).
95. *Id.* at 459.
96. *Id.*
97. *Id.* at 462.
98. *Taylor*, 689 N.E.2d at 703.
99. Justice Sullivan filed a dissenting opinion in which he considered some of Taylor's other statements in addition to the one quoted above by the majority. He concluded that the "four statements, taken together, constituted a sufficiently clear and unambiguous request to have an attorney present [and] that all the questioning should have ceased." *Id.* at 707 (Sullivan, J., dissenting).
100. *Id.* at 703, 704. Taylor also raised an Indiana Constitutional claim, but the court noted that he "offer[ed] no authority contrary to the *Davis* view construing the Indiana constitutional right to counsel, and [the court] discern[ed] no good reason for a different rule." *Id.* at 704.
101. *Id.* at 703.
102. 698 N.E.2d 796 (Ind. 1998).
103. *See id.* at 800-01.
104. 451 U.S. 477 (1981).

which holds that when a defendant invokes his right to counsel, the police must cease questioning until counsel has been made available or until the accused initiates further communication with the police. The court began by noting that the purpose underlying *Miranda* warnings is to protect an individual's privilege against self-incrimination, but that the privilege does not apply to the taking of blood samples.[105] Moreover, the holdings of *Miranda* and *Edwards* were "explicitly limited to circumstances in which an individual is 'subjected to questioning' or 'during custodial interrogation[.]'"[106] Finally, the court quoted from the fairly recent opinion in *McNeil v. Wisconsin*,[107] in which the U.S. Supreme Court observed in dicta that it had "never held that a person can invoke his *Miranda* rights anticipatorily in a context other than 'custodial interrogation' .... Most rights must be asserted when the government seeks to take the action they protect against."[108] Because Sauerheber's request for counsel fell outside of one of the "windows of opportunity" during which a defendant must assert his right to counsel, the police were not prevented under *Edwards* from questioning him four days later, after advising him at that time of his *Miranda* rights and receiving no request for an attorney.[109]

Finally, in *Smith v. State*,[110] the supreme court clarified the standard to be applied when a defendant challenges the voluntariness of a confession under the Fifth Amendment.[111] The court noted that Indiana courts have cited to and applied different standards when evaluating voluntariness issues under the U.S. Constitution. Under U.S. Supreme Court case law, however, the correct standard is the preponderance of the evidence standard.[112] Accordingly, the court overruled several Indiana cases that relied on the beyond a reasonable doubt standard.[113]

C. Dismissal and Refiling of Additional Charges

In *Davenport v. State*,[114] the supreme court considered whether, four days after the denial of a motion to amend the charging information by adding three additional counts, the State could dismiss the original charge and refile it along with the three additional charges. As a general proposition, once an information has been dismissed by the State, it may be refiled subject to certain restrictions.[115]

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105. *Sauerheber*, 698 N.E.2d at 801-02 (citing Schmerber v. California, 384 U.S. 757 (1966)).

106. *Id.* at 802.

107. 501 U.S. 171 (1991).

108. *Sauerheber*, 698 N.E.2d at 802 (quoting *McNeil*, 501 U.S. at 182 n.3).

109. *Id.* at 802-03 (quoting United States v. LaGrone, 43 F.3d 332, 338 (7th Cir. 1994)).

110. 689 N.E.2d 1238 (Ind. 1997).

111. *Id.* at 1246 n.11.

112. *See id.*

113. *Id.*

114. 689 N.E.2d 1226 (Ind. 1997), *modified on reh'g*, 696 N.E.2d 870 (Ind. 1998).

115. *See id.* at 1229.

For example, the State may not refile the same offense if jeopardy has attached or to evade the defendant's speedy trial rights.[116] In this case, however, the court considered whether the filing of additional charges would "prejudice the substantial rights of the defendant."[117] The court held that the State's action

> not only crossed over the boundary of fair play but also prejudiced the substantial rights of the defendant. Because of a sleight of hand, the State was able to escape the ruling of the original court and pursue the case on the charges the State had sought to add belatedly. This is significantly different than what has been permitted in the past.[118]

The court reversed the convictions on the additional charges.[119]

D. Speedy Trial

In *State ex rel. Bishop v. Madison Circuit Court*,[120] the supreme court published a per curiam "Original Action" opinion "to make a more public record of the continuing importance of Criminal Rule 4(C)."[121] That rule provides in material part:

> No person shall be held on recognizance or otherwise to answer a criminal charge for a period in aggregate embracing more than one year from the date the criminal charge against such defendant is filed, or from the date of his arrest on such charge, whichever is later . . . . Any defendant so held shall, on motion, be discharged.[122]

In this case, the defendant appeared in court and pled not guilty to charges of Intimidation and Harassment on May 21, 1996.[123] The case progressed in normal course for about three months when, on August 16, the defendant filed a motion to compel discovery. The State did not file a response until eleven months later—on July 14, 1997—at which time it also requested that a trial date be set.[124] Two days later the defendant filed an objection to the setting of a trial date and a motion for discharge pursuant to Criminal Rule 4(C).[125] The motion was denied, a trial date was set, and the defendant filed an original action with the supreme court.[126] Noting that "[t]here is nothing in the record of proceedings suggesting that the delay in bringing this case to trial—indeed, the delay in even

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116. *See id.*
117. *Id.*
118. *Id.* at 1230.
119. *Id.*
120. 690 N.E.2d 1173 (Ind. 1998).
121. *Id.* at 1174.
122. *Id.* (quoting IND. R. CRIM. P. 4(C)).
123. *See id.* at 1173.
124. *See id.*
125. *See id.* at 1174.
126. *See id.*

setting a trial date—was in any way attributable to the relator," the court issued a writ of mandamus directing his discharge.[127]

The court of appeals also addressed a Criminal Rule 4(C) claim in *Haston v. State*.[128] In that case, the defendant was charged with operating a vehicle while intoxicated on December 10, 1992. On March 23, 1993, he filed a motion to suppress the Breathalyzer test results. The motion was denied on the same day and the trial court certified the ruling for interlocutory appeal.[129] Haston never pursued an interlocutory appeal. On May 15, 1996, the trial court set the case for trial on July 30, 1996, nearly four years after charges were filed.[130] Haston moved for discharge the day before his trial, and that motion was denied.

The State argued that the delay in bringing Haston to trial was attributable to him because he requested but never pursued an interlocutory appeal. The court of appeals noted that under Criminal Rule 4 decisional law defendants are properly charged with the "time from initially seeking an interlocutory appeal to the date an appellate decision is issued."[131] According to the appellate rules, Haston had only thirty days from the certification order in which to petition the court of appeals to entertain his interlocutory appeal.[132] Accordingly, Haston's opportunity to seek appellate review expired by operation of law after thirty days.[133] Although the State argued that it should be granted "equitable time" for its detrimental reliance on Haston's representation that he would be filing an interlocutory appeal, the court of appeals concluded that "this additional time falls woefully short of the approximately two and one-half years required to comply with [Criminal Rule] 4(C) in this case."[134] Because the trial court erred by denying Haston's timely motion for discharge, the court of appeals reversed his convictions.[135]

E. Courtroom Security

The notorious 1996 "Ghetto Boys" trial in Marion County presented the somewhat novel issue of courtroom security procedures to the supreme court. The Ghetto Boys were a group organized to sell crack cocaine, and five of the Ghetto Boys fired at least sixty-five rounds of ammunition from assault rifles at an apartment complex in apparent retaliation against someone who had stolen from the group's stash of cocaine.[136] At the joint trial, members of the public

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127. *Id.*

128. 695 N.E.2d 1042 (Ind. Ct. App. 1998).

129. *See id.* at 1043.

130. *See id.*

131. *Id.*

132. *Id.* (citing IND. R. APP. P. 2(A)).

133. *See id.*

134. *Id.* at 1044 (citation omitted).

135. *Id.* at 1044-45.

136. *See* Williams v. State, 690 N.E.2d 162, 165 (Ind. 1997); *see also* Marbley v. State, 690 N.E.2d 185, 186 (Ind. 1997); Morrow v. State, 690 N.E.2d 183, 184 (Ind. 1997); Ridley v. State,

who sought access to the courtroom were required to pass through a metal detector and "wand" inspection. Spectators who were unknown to the court were also required to present identification to the officer at the door and sign in.[137] On appeal, the defendant challenged these procedures as infringing upon his right to a public trial under the Sixth Amendment.[138] He also challenged the restrictions based on statute, which provides that "[c]riminal proceedings are presumptively open to attendance by the general public."[139]

The court noted the important interests served by a public trial. "[T]he presence of interested spectators may keep [the accused's] triers keenly alive to a sense of their responsibility and to the importance of their functions . . . ."[140] It protects the accused by allowing the public access to scrutinize the fairness of the proceedings, encourages witnesses to come forward, and discourages perjury.[141] The court found no constitutional or statutory violation because these protections "conceive of an exclusion as an affirmative act specifically barring some or all members of the public from attending a proceeding."[142] In this case, however, "[n]either requirement actively exclude[d] anyone. The identification requirement introduced a minor procedural hurdle to gaining admittance to the trial by demanding the production of some form of identification, which is an item readily available to the general public."[143] At most, the procedures may have kept some of Williams' supporters with shady backgrounds away from the proceedings, but the court concluded that there was no evidence or even an allegation as to how these procedures affected the fairness of the proceedings or any of the objectives of the Sixth Amendment.[144]

Although the court found no violation of Williams' Sixth Amendment right, the court stated that "it does not follow that the procedures were justified or properly taken" because of the First Amendment rights of the press and the public to attend the trial.[145] To guard against any future violations of the First Amendment, the court announced a new rule under its supervisory powers that applies to trials conducted after the publication of the opinion.[146] Trial courts

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690 N.E.2d 177, 179 (Ind. 1997).

137. *See Williams*, 690 N.E.2d at 166.

138. *Id.* The supreme court found any challenge to the use of a metal detector or wand to be waived because there was no objection at trial to these measures. Therefore, the court only considered the identification and sign-in and procedures. Moreover, because the defendant made no contention based on the language or history of the Indiana Constitution, the court resolved his state and federal constitutional claim based on federal constitutional doctrine and expressed no opinion as to what, if any, difference there may be under the state constitution. *Id.* at 167.

139. *Id.* (quoting IND. CODE § 5-14-2-2 (1998)).

140. *Id.* (quoting Gannett Co. v. DePasquale, 443 U.S. 368, 380 (1979)).

141. *See id.*

142. *Id.* at 168.

143. *Id.*

144. *Id.*

145. *Id.* at 169.

146. *Id.* at 169-70.

must now "make a finding that specifically supports any measures taken beyond what is customarily permitted . . . . The finding need not be extensive, but must provide the reasons for the action taken, and show that both the burden and benefits of the action have been considered."[147]

F. Jury

1. Deliberations.—In December of 1997, a panel of the court of appeals issued an opinion in *Riggs v. State.*[148] The opinion noted the divergence of opinions of that court regarding what triggers the application of Indiana Code section 34-1-21-6. That statute provides:

> After the jury have retired for deliberations, if there is a disagreement between them as to any part of the testimony, or if they desire to be informed as to any point of law arising in the case, they may request the officer to conduct them into court, where the information required shall be given in the presence of, or after notice to, the partes or their attorneys.[149]

Relying on the plain language of the statute, the *Riggs* court held that "[w]here the jury does not explicitly manifest any disagreement about the testimony or does not ask for clarification of a legal issue, [Indiana Code section] 34-1-21-6 simply does not apply."[150] The court acknowledged that its decision conflicted with opinions from other panels of the court of appeals in two respects. Specifically, the *Riggs* panel noted that "[r]equests by the jury to review exhibits, which are items of physical evidence, are never within the scope of the statute."[151] This conflicts with the view expressed by a different panel of the court of appeals in *Anglin v. State*[152] that requests to review exhibits may sometimes fall within the scope of the statute. Moreover, *Riggs* also held that the statute is not triggered whenever the jury requests to rehear testimony or see exhibits for a second time, but rather only when the jury explicitly manifests disagreement about testimony.[153]

Several months later, the supreme court resolved the split in the court of

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147. *Id.* at 169 (citation omitted).

148. 689 N.E.2d 460 (Ind. Ct. App. 1997).

149. IND. CODE § 34-1-21-6 (1993) (current version at IND. CODE § 34-36-1 (1998)). The 1998 recodification contains only minor editorial changes.

150. *Riggs*, 689 N.E.2d at 463.

151. *Id.* at 462.

152. 680 N.E.2d 883, 885 n.2 (Ind. Ct. App. 1997), *trans. denied*, 690 N.E.2d 1185 (Ind. 1997).

153. *Riggs*, 689 N.E.2d at 463. *Riggs* was written by Judge Friendlander, who not surprisingly expressed similar views a few months later in *Nuckles v. State*, 691 N.E.2d 211 (Ind. Ct. App. 1998), over the concurring opinion of Judge Kirsch. Judge Kirsch wrote *Winters v. State*, 678 N.E.2d 405 (Ind. Ct. App. 1997), which held that the statute was triggered whenever the jury makes a request during deliberations.

appeals on the latter issue. In *Bouye v. State*, the jury sent a note that read "Deborah's testimony" to the trial judge during deliberations.[154] The court responded, without first informing the defendant or his counsel, with a note that said no transcripts were available.[155] On appeal, the defendant contended that this ex parte communication violated Indiana Code section 34-1-21-6. The supreme court characterized the split in the court of appeals as follows: "One line holds that, where the jury does not *explicitly* manifest any disagreement about the testimony or does not ask for clarification of a legal issue, the statute does not apply."[156] However, "[t]he other line holds that, whenever a jury requests that it be given the opportunity to rehear testimony for a second time, the jury is *inherently* expressing disagreement or confusion about that evidence, thus triggering the statute *any* time a jury makes a request for testimony."[157] Relying on the plain language of the statute, the supreme court found the first line cases more persuasive and divined that the legislature's intent was to limit the statute's application to those cases "in which the jury explicitly indicated a disagreement."[158] Because the jury note in *Bouye* did not indicate disagreement regarding testimony, the statute was not implicated.[159]

A couple of months later, the supreme court applied the rule announced in *Bouye* to a case involving a request to review exhibits after deliberations had begun. In *Robinson v. State*,[160] the court held that the statute was not triggered because the jury's note merely requested the exhibits and did not "explicitly indicate[] a disagreement"[161] The court also noted the division on the court of appeals regarding whether the statute can ever be triggered by a request for exhibits, or instead is triggered only by a disagreement about testimony.[162] *Robinson* did not resolve that issue, but instead rested on the rule announced in *Bouye*. The court also held that the same standards that apply to the trial court's decision to send exhibits to the jury room before deliberations begin also apply to the decision to send exhibits to the jury room after deliberations have begun.[163]

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154. 699 N.E.2d 620, 627 (Ind. 1998).

155. *See id.*

156. *Id.* (citing *Riggs*, 689 N.E.2d at 460; Johnson v. State, 674 N.E.2d 180 (Ind. Ct. App. 1996); State v. Chandler, 673 N.E.2d 482 (Ind. Ct. App. 1996); Jones v. State, 656 N.E.2d 303 (Ind. Ct. App. 1995)) (emphasis in original).

157. *Id.* (citing Anglin v. State, 680 N.E.2d 883 (Ind. Ct. App. 1997); State v. Winters, 678 N.E.2d 405 (Ind. Ct. App. 1997)) (emphasis in original).

158. *Id.* at 627-28.

159. *Id.* at 628.

160. 699 N.E.2d 1146 (Ind. 1997).

161. *Id.* at 1149.

162. *Id.*

163. *Id.* at 1150. In so holding the court cited *Ingram v. State*, 547 N.E.2d 823, 828-29 (Ind. 1989), *Roland v. State*, 501 N.E.2d 1034, 1040 (Ind. 1986), *Torres v. State*, 442 N.E.2d 1021, 1025-26 (Ind. 1982), and *Pearson v. State*, 441 N.E.2d 468, 476 (Ind. 1982), all cases that applied the ABA standard adopted in *Thomas v. State*, 289 N.E.2d 508 (Ind. 1972), to jury requests made after deliberations had begun.

The test, which was first adopted in *Thomas v. State*,[164] is: "'(i) whether the material will aid the jury in a proper consideration of the case; (ii) whether any party will be unduly prejudiced by submission of the material; and (iii) whether the material may be subjected to improper use by the jury.'"[165] The trial court in *Robinson* properly considered these three factors, and therefore did not err by sending the requested photographs to the jury room after deliberations had begun.[166] As a final point, the supreme court held that the defendant's right to be present under both the state and federal constitutions was not violated by sending exhibits to the jury room in the absence of the defendant.[167]

2. Size.—In *Henderson v. State*,[168] the supreme court resolved another conflict between two decisions of the court of appeals. That conflict concerned whether a defendant charged with a misdemeanor or Class D felony offense that is enhanced to a Class C felony based on a prior conviction is to be tried by a jury of six or twelve. According to statute, when an individual is tried by jury on misdemeanor or Class D felony charges, the jury consists of six jurors.[169] An individual charged with a Class C felony or higher offense, however, must statutorily be tried by a jury of twelve.[170] The court held that "when the State's charging instrument charges the defendant with a Class C felony or higher, regardless of whether the charge has been elevated by virtue of a prior conviction, a twelve-person jury is required."[171]

G. Lesser Included Offenses

The standards by which a trial court determines whether to accept a party's instructions on lesser included offenses is well established. Under the test established in *Wright v. State*,[172] the court must first decide whether the lesser included offense is either inherently or factually included within the crime charged in the information.[173] If the lesser included offense is inherently or

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164. 289 N.E.2d 508 (Ind. 1972).

165. *Robinson*, 699 N.E.2d at 1150 (quoting *Thomas*, 289 N.E.2d at 509).

166. *See id.*

167. *Id.* at 1150-51.

168. 690 N.E.2d 706 (Ind. 1998).

169. *See id.*; *see also* IND. CODE § 35-37-1-1(b) (1998).

170. *See Henderson*, 690 N.E.2d at 706.

171. *Id.* at 707. The court of appeals cited *Henderson* several months later when considering the applicable statute of limitations for a Class D felony, enhanced dealing in marijuana charge. *See* Lamb v. State, 699 N.E.2d 708 (Ind. Ct. App.), *trans. denied*, No. 48A02-9712-CR-847 (Ind. Nov. 4, 1998). The defendant in *Lamb* was charged with a Class A misdemeanor enhanced to a Class D felony by virtue of a prior conviction. The court of appeals held that the five year felony statute of limitations, rather than the two year misdemeanor statute of limitations, applied to his case. However, "if the State proves all the elements of felony dealing except a prior conviction, [the defendant] shall not be convicted of felony dealing or misdemeanor dealing." *Id.* at 711.

172. 658 N.E.2d 563 (Ind. 1995).

173. *See* Young v. State, 699 N.E.2d 252, 255 (Ind. 1998) (citing *Wright*, 658 N.E.2d at 563).

factually included, the trial court must then consider whether the evidence presented at trial creates a serious evidentiary dispute about the element or elements that distinguish the greater from the lesser offense.[174] The failure to give a properly tendered instruction when a serious evidentiary dispute exists is reversible error if a jury could conclude that the lesser offense was committed but not the greater.[175]

In *Young v. State*, the defendant was charged with murder and presented an alibi defense at trial.[176] Nevertheless, he also sought to have the jury instructed as to the lesser included offenses of reckless homicide and involuntary manslaughter. The trial court made no findings regarding whether a serious evidentiary dispute existed on the issue of Young's mens rea, but simply stated that Young was not entitled to lesser included instructions because he raised an alibi defense.[177] The supreme court noted that "[p]resenting an alibi defense does not automatically bar instructions on a lesser included offense."[178] As to the proffered lesser included instruction for reckless homicide, the court concluded that there was a genuinely disputed issue as to whether Young knowingly or recklessly killed.[179] Young fired shots from a car in the general direction of a number of people in front of a house, but trial testimony differed as to whether he was aiming at any particular person or people, or was just engaged in random shooting.[180] Because refusing the instruction denied the jury its prerogative to decide this question of fact, the court remanded the case for a new trial.[181] As to the involuntary manslaughter instruction, however, the court held that it was properly refused because there was no serious evidentiary dispute regarding whether Young "recklessly, knowingly, or intentionally inflicted serious bodily injury on another person, and killed that person in the course of such acts."[182] Young knew the gun was loaded, realized people were standing in the general direction of his firing, shouted taunting words, and returned and fired more shots after the initial shooting.[183]

H. Habitual Offender

The supreme court decided a pair of cases that considered the jury's role during a habitual offender phase of a trial. Both cases were decided based on the Indiana constitutional provision that "[i]n all criminal cases whatever, the jury

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174. *See id.* (citing *Wright*, 658 N.E.2d at 563).
175. *See id.*
176. *Id.* at 256.
177. *See id.* at 255-56.
178. *Id.* at 256.
179. *See id.* at 257; *see also* IND. CODE § 35-41-2-2(c) (defining recklessly).
180. *Young*, 699 N.E.2d at 254.
181. *Id.* at 257.
182. *Id.*; *see also* IND. CODE § 35-42-1-4 (1998).
183. *See Young*, 699 N.E.2d at 257.

shall have the right to determine the law and the facts."[184] In *Seay v. State*,[185] the court described the issue as follows:

> [W]hether the jury in a habitual offender proceeding is permitted to render a verdict that the defendant is not a habitual offender even if it finds that the Sate has proved beyond a reasonable doubt that the defendant has accumulated two prior unrelated felonies. That is, is the jury entitled to make a determination of habitual offender status as a matter of law independent of its factual determinations regarding prior unrelated felonies?[186]

The court noted that it was "difficult to reconcile" some of its prior decisions on the issue, but then adopted the principles enunciated by Justice Dickson in his concurring and dissenting opinions in two earlier cases.[187] Specifically, the verdict form used during a habitual offender phase must allow the jury not only to "determine whether the defendant has been twice previously convicted of unrelated crimes, but [the jury] must further determine whether such two convictions, when considered along with the defendant's guilt of the charged crime, lead them to find that the defendant is a habitual criminal."[188] The court also considered legislative intent on the issue. "If the legislature had intended an automatic determination of habitual offender status upon the finding of two unrelated felonies, there would be no need for a jury trial on the status determination."[189]

The court found that the instructions at issue in *Seay* were erroneous,[190] but the analysis did not end there. In *Seay*, the issue was presented in a post-conviction proceeding in which the defendant contended that it was fundamental error for the trial court to give the erroneous instruction. The defendant also argued that he was denied the effective assistance of counsel when trial counsel did not object to the instruction and when appellate counsel did not raise a claim of fundamental error on direct appeal.[191] The court summarily affirmed the court of appeals' finding that no fundamental error resulted from the giving of the instructions and that trial and appellate counsel were not ineffective.[192]

In *Parker v. State*,[193] decided on the same day as *Seay*, the supreme court considered the same issue in the context of a criminal direct appeal. Parker

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184. IND. CONST. art. I, § 19.

185. 698 N.E.2d 732 (Ind. 1998).

186. *Id.* at 734.

187. *Id.* at 735-36.

188. *Id.* at 736 (quoting Duff v. State, 508 N.E.2d 17, 23 (Ind. 1987) (Dickson, J., separate opinion)).

189. *Id.* (citing Hensley v. State, 497 N.E.2d 1053, 1058 (Ind. 1986) (Dickson, J., concurring and dissenting)).

190. *Id.* at 737.

191. *See id.*

192. *Id.*; *see also* Seay v. State, 673 N.E.2d 475 (Ind. Ct. App. 1996).

193. 698 N.E.2d 737 (Ind. 1998).

contended that "the trial court erred by instructing the jury that if it found that the State had proved the predicate felonies, it 'should' find him to be a habitual offender."[194] The court observed that this type of instruction "prevented the jury from making an independent and separate decision on habitual offender status,"[195] which was exactly the result its decision in *Seay* was aimed at preventing.[196] However, "reversible error does not necessarily occur when the type of instruction provided in this case is accompanied by another instruction informing the jury that it is the judge of the law and the facts."[197] Nevertheless, the court found that giving the instruction under the particular circumstances of the case to be reversible error.[198] Specifically, the trial court

> both (i) provided over defendant's objection an instruction which minimized the jury's power of discretion in making a determination on habitual offender status, and (ii) refused over defendant's objection to re-read the guilt phase instruction (which had been delivered two weeks earlier) advising the jury that it was the judge of both the law and the facts.[199]

In a different context the supreme court also held in *Leach v. State*[200] that is was error to inform prospective jurors during voir dire that a defendant is charged "with being a Habitual Criminal Offender."[201] The court noted that "[t]he defendant's criminal history was not directly relevant to an issue in the guilt phase, and, therefore, the trial court's comments were clearly improper."[202] Nevertheless, the court held that the error was "a trial error rather than a structural error," and therefore subject to harmless error analysis.[203] Although noting that "the trial court's comments regarding the habitual offender charge were improper and prejudicial and that, in almost any other instance, such comments would be reversible error," the supreme court found the error to be harmless because "the evidence of guilt was so overwhelming."[204]

I. Selling a Handgun to a Minor

In *State v. Shelton*,[205] the court of appeals considered whether the legislature intended for the sale of a handgun to a minor to be a strict liability offense in

194. *Id.* at 741.
195. *Id.* at 742.
196. *Id.*
197. *Id.*
198. *Id.* at 743.
199. *Id.*
200. 699 N.E.2d 641 (Ind. 1998).
201. *Id.* at 642.
202. *Id.* at 643.
203. *Id.*
204. *Id.* at 644.
205. 692 N.E.2d 947 (Ind. Ct. App. 1998).

which no culpable mental state need be proven.[206] After Andrew Spalding pled guilty to Reckless Homicide and Carrying a Handgun Without a License, he identified Shelton as the person who sold him the handgun used to commit these offenses.[207] Shelton was charged with Selling a Handgun to a Minor, a Class C felony.[208] In material part, that offense is defined as "a person may not sell, give, or in any manner transfer the ownership or possession of a handgun or assault weapon (as defined in [Indiana Code section] 35-50-2-11) to any person under eighteen years of age."[209] The statute does not specify a culpable mental state. The trial court, over the objection of the State, instructed the jury that the State was required to prove that "the defendant knowingly or intentionally sold a handgun to a person under the age of eighteen."[210] The court of appeals noted that "other statutes which ban the sale of certain items to minors explicitly state the culpable mental state required for a conviction."[211] Although courts presume that the legislature intended to include a culpable mental state in a criminal statute, that presumption may be overcome if the following factors decisively indicate that no mental state was intended:

> 1. the legislative history, title of context of the criminal statute;
> 2. similar or related statutes;
> 3. the severity of punishment (greater penalties favor culpable mental state requirement);
> 4. the danger to the public of prohibited conduct (greater danger disfavors need for culpable mental state requirement);
> 5. the defendant's opportunity to ascertain the operative facts and avoid the prohibited conduct;
> 6. the prosecutor's difficulty in proving the defendant's mental state; and
> 7. the number of expected prosecutions (greater numbers suggest that crime does not require culpable mental state).[212]

Of these seven factors, the court found that only two "militate against the imposition of strict liability, (1) the severity of the punishment and (2) the expected number of prosecutions."[213] The court concluded that

> youths with handguns present a great danger both to our youth and the general public, which weighs heavily in favor of the conclusion that the legislature intended to make the sale or transfer of a handgun to a person less than eighteen years of age a strict liability offense. That is especially true when considered the ease with which a defendant can

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206. *Id.* at 949.
207. *See id.* at 948.
208. *See id. See also* IND. CODE § 35-47-2-7 (1998).
209. IND. CODE § 35-47-2-7(a) (1998).
210. *See Shelton*, 692 N.E.2d at 951.
211. *Id.* at 950.
212. *See id.* at 949 (quoting State v. Keihn, 542 N.E.2d 963, 967 (Ind. 1989)).
213. *Id.* at 950.

> ascertain the transferee's age. The two factors which militate against that conclusion are insufficient to overcome it. We conclude that the legislature did not intend to require a culpable mental state.[214]

Although the trial court erred when it determined that the State was required to prove that Shelton knew that Spalding was under the age of eighteen, retrial was barred because Shelton was acquitted at trial.[215]

J. Probation

The court of appeals considered a variety of issues relating to probation. Three of those are discussed here. In *Wright v. State*,[216] the defendant appealed the revocation of his probation based on the alleged violation of a no-contact order. Wright had been convicted of intimidation and harassment for threatening the life of a doctor who refused to prescribe a controlled substance for him.[217] As a condition of his probation, Wright was prohibited from contacting the doctor or any member of the doctor's family. Nevertheless, Wright filed a complaint against the doctor alleging negligence, destruction of the doctor/patient relationship, and harassment.[218] A summons, complaint, and set of interrogatories were all served on the doctor. The State sought and obtained revocation of Wright's probation on the basis that filing a lawsuit was an indirect written communication, which was prohibited by the no-contact order.[219] The court of appeals reversed the trial court, noting that "the purpose of the no-contact order was to prevent Wright form harassing and intimidating" the doctor and his family.[220] Because the court could not conclude that the complaint was filed merely to harass the doctor, absent a determination that it is frivolous or groundless, the court held that the State failed to present sufficient evidence that Wright violated the no-contact order.[221]

In *Bell v. State*,[222] the court of appeals considered whether a defendant was denied his right to due process when the trial court failed to determine whether his decision to proceed without counsel at his probation revocation hearing was voluntary.[223] While on probation, Bell was charged with public intoxication and pled guilty to that charge. The court held an evidentiary hearing on the probation violation at which the State presented evidence of Bell's new conviction.[224] Bell's probation was revoked and he was ordered to execute his previously

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214. *Id.* at 950-51.
215. *See id.* at 951.
216. 688 N.E.2d 224 (Ind. Ct. App. 1997).
217. *See id.* at 225.
218. *See id.*
219. *See id.*
220. *Id.* at 226.
221. *Id.*
222. 695 N.E.2d 997 (Ind. Ct. App. 1998).
223. *Id.* at 998.
224. *See id.*

suspended sentence.[225] Bell was not represented by counsel at the revocation hearing or when he pleaded guilty to the public intoxication charge.[226]

The court of appeals noted the well-established rule that "whenever a defendant proceeds without the benefit of counsel, the record must reflect that the right to counsel was voluntarily, knowingly, and intelligently waived."[227] In this case, however, the record did not show that the trial court advised Bell of his right to counsel nor did it determine that his waiver was voluntary.[228] The court observed that it "was under no illusion that the outcome of the probation revocation hearings would have been any different had Bell been represented by counsel."[229] However, because invalid waivers of counsel are not subject to harmless error analysis, the court reversed the revocation of probation and remanded for a new hearing that complies with the requirements of due process.[230]

Finally, in *Williams v. State*,[231] the court of appeals considered whether a defendant's *Alford* plea in another state was sufficient to support the revocation of his probation for committing further criminal offenses. An *Alford* plea is a guilty plea where the defendant accepts punishment but denies guilt.[232] Indiana has specifically declined to accept *Alford* pleas from defendants.[233] Nevertheless, Williams entered an *Alford* plea to charges in Kentucky, and the State presented certified documents to the Indiana court supervising his probation showing that he had entered this plea.[234] The court of appeals observed that "[u]nder Kentucky law, an *Alford* plea is a guilty plea and clearly constitutes a conviction, the defendant's protestations of innocence notwithstanding."[235] Moreover, probation revocation under Indiana law "may be based upon evidence of the commission of an offense, even if the probationer has been acquitted of the crime after trial."[236] Accordingly, the court affirmed the revocation of Williams' probation.[237]

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225. *See id.*
226. *See id.* at 998-99.
227. *Id.* at 998.
228. *Id.* at 999.
229. *Id.*
230. *Id.*
231. 695 N.E.2d 1017 (Ind. Ct. App. 1998).
232. *Id.* at 1018 n.2 (citing North Carolina v. Alford, 400 U.S. 25 (1970)).
233. *See id.* at 1018.
234. *See id.*
235. *Id.*
236. *Id.* at 1019 (citing Justice v. State, 550 N.E.2d 809, 812 (Ind. Ct. App. 1990)).
237. *Id.*

RECENT DEVELOPMENTS IN INDIANA EVIDENCE LAW

JEFFREY O. COOPER*

It is now more than five years since the Indiana Rules of Evidence (the "Rules") went into effect on January 1, 1994. In that time, the Indiana courts have occasionally struggled to adjust to the changes in Indiana's evidence law wrought by the Rules. This past year saw a number of significant decisions under the Rules. Some of those decisions, however, raised as many questions as they answered.

This Article analyzes the major developments in Indiana evidence law during the period between October 1, 1997 and September 30, 1998. The organization of the Article parallels the structure of the Indiana Rules of Evidence.

I. SCOPE—RULE 101

A. *Preemption of Common Law and Statutory Law*

Rule 101(a) provides that the Indiana Rules of Evidence apply in all Indiana court proceedings "except as otherwise required by the Constitution of the United States or Indiana, by provisions of this rule, or by other rules promulgated by the Indiana Supreme Court."[1] The Rule further provides that, if no Rule of Evidence covers a particular question, statutory or common law shall apply.[2] Although the Rule does not expressly preempt statutes that conflict with a provision of the Rules, such preemption is plainly implied, and the Indiana Supreme Court has held on several occasions that, where a statute and a Rule of Evidence conflict, the Rule of Evidence shall apply.[3]

In *McEwan v. State*,[4] the Indiana Supreme Court addressed such a conflict. *McEwan* was a murder prosecution in which the defendant was accused of stabbing his girlfriend in the chest. During its case-in-chief, the prosecution offered evidence that, three months prior to the homicide, the defendant and the victim had engaged in a fight that had ended as the victim fled in the car of a friend and the defendant fired several gunshots at the car.[5] The defendant argued that the introduction of this evidence constituted error because the prosecution had failed to comply with the notice provisions of Indiana Code section 35-37-4-14(d).[6] The statute provides that, if the prosecution wishes to introduce evidence of a prior battery, the state must file a motion, together with an offer of proof, not less than ten days before the beginning of the trial.[7] There was no question in

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* Assistant Professor of Law, Indiana University School of Law—Indianapolis. A.B., Harvard University; J.D., University of Pennsylvania.

1. IND. R. EVID. 101(a).
2. *Id.*
3. *See* Williams v. State, 681 N.E.2d 195, 200 n.6 (Ind. 1997); Humbert v. Smith, 664 N.E.2d 356, 357 (Ind. 1996).
4. 695 N.E.2d 79 (Ind. 1998).
5. *See id.* at 84.
6. *See id.* at 88.
7. *See id.*; *see also* IND. CODE § 35-37-4-14(d) (1998).

McEwan that the prosecution failed to provide the notice required by the statute.[8]

On appeal, the supreme court analyzed whether the statute conflicted with the provisions of the Indiana Rules of Evidence. On the requirement of notice, the court found no conflict. Rule 404(b), covering the admission of other crimes, wrongs, or acts under the Rules, requires the prosecution to give notice to the accused only if the accused requests such notice.[9] This provision, the court concluded, did not foreclose the statutory requirement that notice be given even in the absence of a request.[10] The court noted, however, that other provisions of the statute did conflict with Rule 404(b). Specifically, the statute provided that "evidence of a previous battery is admissible into evidence in the state's case-in-chief for purposes of proving motive, intent, identity, or common scheme and design."[11] Although the purposes for which such evidence might be admissible were compatible with the purposes enumerated in Rule 404(b), the court found troublesome the statutory provision that such evidence "is admissible."[12] The court noted that Rule 403 of the Indiana Rules of Evidence allowed for the admission of evidence only upon a balancing of probative value against the danger of unfair prejudice.[13] Because the statute did not allow for consideration of prejudicial effect, but rather provided that evidence of prior batteries "is admissible," the statute would appear to allow for the introduction of evidence that would be barred by the Indiana Rules of Evidence. The statute was therefore preempted on the point of conflict.[14] Further, because the notice provisions could not be severed from the voided provisions of the statute, the notice provision was preempted as well.[15]

The implications of the *McEwan* decision are not entirely clear. Rule 403 applies generally to the admission of evidence under the Indiana Rules. *McEwan* therefore might be read to preempt any statutory provision that calls for the admission of evidence without weighing probative value against prejudicial effect. Interpreted this way, *McEwan's* effect would be sweeping indeed. The decision, however, might properly be read more narrowly. In *Hicks v. State*,[16] the Indiana Supreme Court incorporated Rule 403 balancing directly into the inquiry under Rule 404(b).[17] *Hicks* suggests that Rule 403 balancing has a special role in determining whether evidence is admissible under Rule 404(b), above and beyond the role it plays generally. Taking *Hicks* into account, it is possible to read *McEwan* narrowly. Because the *McEwan* court did not cite *Hicks*, however, it is unclear how far the supreme court intended its decision to reach.

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8. *See Williams*, 695 N.E.2d at 88.
9. IND. R. EVID. 404(b).
10. *McEwan*, 695 N.E.2d at 88.
11. IND. CODE § 35-37-4-14(c).
12. *McEwan*, 695 N.E.2d at 88-89.
13. *Id.* at 87.
14. *See id.* at 89.
15. *See id.*
16. 690 N.E.2d 215 (Ind. 1997).
17. *Id.* at 219; *see infra* notes 77-78 and accompanying text.

If the ramifications of the supreme court's decision in *McEwan* are somewhat uncertain, the reasoning of the Indiana Court of Appeals in *State v. Walton*[18] is little short of baffling. In *Walton*, the court addressed whether a defendant in a rape prosecution has the right to present evidence that the victim made a prior false accusation of rape. Prior to the adoption of the Rules, the Indiana Supreme Court had held that a defendant was entitled to present such evidence where (1) the victim admitted that her prior accusation was false, or (2) the prior accusation was "demonstrably false."[19] At issue in *Walton* was whether this entitlement survived the adoption of the Rules.[20]

The *Walton* court recognized that two Rules arguably addressed the admissibility of evidence of prior false accusations of rape: Rule 412, the so-called rape shield rule, prohibits the introduction, with narrow exceptions, of evidence of the victim's sexual history in prosecutions for rape or sexual misconduct,[21] while Rule 608(b) regulates methods of attacking a witness's credibility, providing that, except for evidence of criminal convictions, a witness's credibility may not be attacked or supported through extrinsic evidence of specific instances of conduct.[22] Although the court noted legal commentary that questioned whether the adoption of the Rules invalidated the decisions allowing the sexual offense defendant to show that the victim had made prior false accusations of rape,[23] the court concluded that neither Rule 412 nor Rule 608(b) served as a bar to the evidence. First, the court asserted, both Rule 412 and Rule 608(b) represented restatements of the prior law (common law in the case of Rule 608(b), common law and statutory law in the case of Rule 412).[24] As the exceptions existed at common law and were not foreclosed by statutory law, they remained in force under the Rules. Second, the court reasoned, Rule 608(b) did not cover the specific evidentiary issue presented by prior false accusations of rape; therefore, under Rule 101(a), prior common law remained in effect.[25]

The court's reasoning is highly problematic. First, it is one thing to say that particular Indiana Rules of Evidence are consistent with the basic approach taken by the law as it existed prior to the adoption of the Rules, and quite another to say that, where such consistency exists, the Rules adopt *sub silencio* all the exceptions that were recognized under the prior law. Even the *Walton* court recognized, in a footnote, that where differences existed between Rule 412 and

18. 692 N.E.2d 496 (Ind. Ct. App.), *trans. granted*, 698 N.E.2d 496 (Ind. 1998).

19. Stewart v. State, 531 N.E.2d 1146, 1149 (Ind. 1988).

20. *Walton*, 692 N.E.2d at 499.

21. IND. R. EVID. 412.

22. IND. R. EVID. 608(b).

23. *Walton*, 692 N.E.2d at 499 n.6 (citing Robert L. Miller, *Indiana Evidence*, IND. PRACTICE § 608.207, at 150 (2d ed. 1995)).

24. *Id.*

25. *Id.* at 500.

Indiana's Rape Shield Statute,[26] the Rule controlled.[27] Second, the conclusion that Rule 608(b) does not address the issue raised by evidence of prior false accusations of rape is simply untenable, given the rationale for allowing such evidence that the court asserts: The importance of credibility determinations in sexual misconduct cases. If the purpose of allowing the defendant to offer evidence that the victim of the alleged sexual misconduct made prior false accusations is to undermine the victim's credibility, then Rule 608(b) plainly and squarely applies: The Rule states that prior specific instances of conduct that go to such credibility may be inquired into on cross-examination but may not be established through extrinsic evidence. To state that Rule 608(b) does not take into account the particular concerns that might arise in the narrow context of prosecutions for sexual misconduct is no answer because this will always be true where the common law or statutory law has carved out a narrow exception to a general rule. But the approach to Rule 101(a) taken by the supreme court in *McEwan* forecloses this interpretation because in *McEwan* the supreme court held that a special statutory rule governing the admissibility of evidence of a prior battery was preempted by the general approach taken by Rule 404(b) to the admission of other acts as substantive evidence. This is true despite any special concerns presented by evidence of prior batteries that might have prompted the narrow statutory rule.[28]

It might, under the Rules, be defensible to allow a defendant in a sexual misconduct prosecution to attack the charges against him by asking the alleged victim about prior false accusations of rape, and by introducing extrinsic evidence of the demonstrably false allegations if the victim denies them. It might, for example, be suggested that, in sexual misconduct prosecutions, a victim's history of fabrication does not simply go to the victim's credibility but rather constitutes direct evidence of a defense of fabrication,[29] and that Rule 608(b)'s limitations on extrinsic evidence therefore do not apply. Or it might be argued that the Confrontation Clause of the Sixth Amendment requires that the defendant be allowed to present extrinsic evidence of prior false accusations to impeach the victim's testimony.[30] But the approach taken by *Walton* is not tenable; indeed, it threatens to undo the primacy of the Rules that the Indiana Supreme Court has explicitly recognized.[31] The Indiana Supreme Court has granted transfer in *Walton*, and it must be hoped that the court's resolution will

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26. IND. CODE § 35-37-4-4 (1998).

27. State v. Walton, 692 N.E.2d 496, 500 n.7 (Ind. Ct. App.), *trans. granted*, 698 N.E.2d 496 (Ind. 1998).

28. McEwan v. State, 695 N.E.2d 79, 88-89 (Ind. 1998); *see supra* notes 4-17 and accompanying text.

29. *See* Manlove v. Sullivan, 775 P.2d 237, 241 n.2 (N.M. 1989). The *Manlove* decision was itself highly problematic, as the Tenth Circuit explained in *Manlove v. Tansy*, 981 F.2d 473, 478 & n.5 (10th Cir. 1992).

30. *See* Hogan v. Hanks, 97 F.3d 189, 191 (7th Cir. 1996) (noting that this argument has never been adopted by the United States Supreme Court or by any federal court of appeals).

31. *See, e.g.*, Williams v. State, 681 N.E.2d 195, 200 n.6 (Ind. 1997).

restore some sense of order to Rule 101(a) jurisprudence.

B. Applicability of the Rules in Particular Proceedings

Rule 101(c)(2) provides that the Rules of Evidence do not apply, inter alia, in "[p]roceedings relating to . . . sentencing, probation, or parole."[32] The Indiana Court of Appeals has struggled with the implications of this provision. In particular, the court has split over whether hearsay is admissible in probation revocation proceedings. The question first arose in *Greer v. State*.[33] In *Greer*, the court concluded that, because the Indiana Rules of Evidence did not apply, the court was bound by Rule 101(a) to look to applicable common law or statutory law.[34] Although no statutory provision applied, the common law in place prior to the 1994 adoption of the Indiana Rules of Evidence had not allowed the use of hearsay in probation hearings.[35] The court therefore reasoned that the combined effect of Rule 101(c)(2), Rule 101(a), and the common law meant that hearsay remained excluded from probation revocation hearings.[36]

Greer might have resolved the issue, but the supreme court vacated the court of appeals' opinion on jurisdictional grounds in 1997.[37] In the vacuum created by the vacating of *Greer*, the court of appeals has split. In *Sutton v. State*,[38] the court, in a curious twist of logic, concluded that by stating that the Indiana Rules of Evidence do not apply in probation revocation hearings, Rule 101(c)(2) itself overturned the common-law decision that barred the use of hearsay in such proceedings.[39] The *Sutton* court thus apparently read Rule 101(c)(2) to mean not only that the Indiana Rules of Evidence did not apply in the enumerated proceedings, but that *no* rules of evidence, whether derived from statutory or common law, applied in such proceedings. In reaching this conclusion, the *Sutton* court did not consider what effect, if any, Rule 101(a) might have.

In *Jones v. State*,[40] Judge Friedlander, in an opinion announcing the court's result, cited *Sutton* with approval and without further comment.[41] A majority of the *Jones* panel, however, refused to follow *Sutton*. Judge Sullivan, joined by Judge Kirsch, concluded that *Sutton* misread the import of the supreme court's vacation of *Greer* on jurisdictional grounds, noting that the supreme court did not address the merits of *Greer's* analysis of Rule 101.[42] Judge Sullivan

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32. IND. R. EVID. 101(c)(2).

33. 669 N.E.2d 751 (Ind. Ct. App. 1996), *vacated*, 685 N.E.2d 700 (Ind. 1997).

34. *Id.* at 755.

35. *Id. See* Payne v. State, 515 N.E.2d 1141, 1144 (Ind. Ct. App. 1987).

36. *Greer*, 669 N.E.2d at 755. For further discussion of *Greer*, see Jeffrey O. Cooper, *Recent Developments Under the Indiana Rules of Evidence*, 30 IND. L. REV. 1049, 1049-51 (1997).

37. Greer v. State, 685 N.E.2d 700 (Ind. 1997).

38. 689 N.E.2d 452 (Ind. Ct. App. 1997).

39. *Id.* at 455.

40. 689 N.E.2d 759 (Ind. Ct. App. 1997).

41. *Id.* at 761.

42. *Id.* at 763.

therefore concluded that hearsay should not be admitted in probation revocation proceedings.

A third panel also followed *Greer*. *Cox v. State*[43] involved revocation of placement in a work release center, rather than revocation of probation, but the court concluded that the same standards should apply in the two types of proceedings.[44] In *Cox*, as in *Jones*, the court looked beyond the bald statement of Rule 101(c)(2) that the Indiana Rules of Evidence do not apply to probation revocation proceedings, and looked to the underlying policy, first set forth ten years earlier in *Payne v. State*,[45] that probationers deserved no less protection from unreliable evidence than did civil litigants.[46] In an opinion issued shortly before this survey went to press, however, the Indiana Supreme Court reversed, and in doing so rejected its prior opinion in *Payne*.[47] The court concluded that the adoption of the Indiana Rules of Evidence, and Rule 101(c) in particular, meant that the rules against hearsay (regardless of their source) do not apply in either probation revocation proceedings or community corrections placement revocation proceedings.[48] Under the supreme court's decision, any relevant evidence, including hearsay, may be considered provided that it bears "some substantial indicia of reliability."[49]

II. Relevance

A. Rule 403: Probative Value Versus Prejudicial Effect

To be admissible under the Indiana Rules, evidence must be relevant—that is, it must make a material fact more or less probable than the fact would be in the absence of such evidence.[50] That evidence is relevant does not guarantee its admissibility, of course—the Rules set forth numerous limitations on the admissibility of relevant evidence and on the purposes for which it can be used. One overarching restriction applies to virtually all evidence: Rule 403 provides that, even if relevant, evidence should not be admitted "if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues, or misleading the jury, or by considerations of undue delay, or needless presentation of cumulative evidence."[51]

Photographs of crime victims and crime scenes frequently raise issues under Rule 403. The presentation of evidence through visual aids such as photographs has the potential to make an emotional impact on the jury—to elicit feelings of

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43. 686 N.E.2d 181 (Ind. Ct. App. 1997), *rev'd*, 706 N.E.2d 547 (1999).
44. *Id.* at 184.
45. 515 N.E.2d 1141 (Ind. Ct. App. 1987).
46. *Cox*, 686 N.E.2d at 185.
47. *See* Cox v. State, 706 N.E.2d 547, 550-51 (Ind. 1999).
48. *See id.*
49. *Id.* at 551.
50. *See* IND. R. EVID. 401, 402.
51. IND. R. EVID. 403.

disgust, outrage, fear, or revulsion—that witness testimony frequently cannot match. The potential for a potent visceral reaction is particularly strong where the photographs depict gruesome wounds and injuries. Because a visceral reaction is not a proper basis for a jury decision,[52] exclusion of such evidence is sometimes warranted. Gruesome photographs are not excluded *per se* under Rule 403,[53] but a careful weighing of probative value is important to ensure that the photographs are being presented for a proper purpose, and not simply "to inflame the jury against [the defendant]."[54]

In two recent decisions, the Indiana Supreme Court addressed the use of photographs depicting crime victims; in each case, the court rejected the defendant's challenge to the photographs' admission. In *Robinson v. State*,[55] a murder prosecution, the state offered photographs depicting the victim's body as it was found, badly decomposed and partially eaten by animals, three weeks after the crime. The court first suggested that, despite the grisly nature of the photographs, their admission was justified to explain "why the State had to resort to extraordinary methods to identify the body, and that the body was identified as [the murder victim]."[56] It is unclear how the photographs could have served the latter purpose, however, because the state's own forensic pathologist testified that the body was so badly decomposed that it could not be identified through ordinary means.[57] As to the former point, the photographs were cumulative, because the state also presented a videotape of the crime scene (to which the defendant did not object).[58] Rather than analyze the probative value and prejudicial effect further, however, the court simply stated in conclusory fashion that any error in admitting the photographs was harmless.[59] At no point did the court make a serious effort to discern the degree of unfair prejudice that the defendant might have suffered.[60]

In *Young v. State*,[61] the court again found no reversible error in the admission of a gruesome photograph depicting a victim at the crime scene, even though the

52. *See* United States v. Fawley, 137 F.3d 458, 466 (7th Cir. 1998).

53. *See* Robinson v. State, 693 N.E.2d 548, 553 (Ind. 1998).

54. Gomez v. Ahitow, 29 F.3d 1128, 1139-40 (7th Cir. 1994) (quoting Ferrier v. Duckworth, 902 F.2d 545, 548 (7th Cir.), *cert. denied*, 498 U.S. 988 (1990)).

55. 693 N.E.2d 548 (Ind. 1998).

56. *Id.* at 553.

57. *Id.* The victim was identified through DNA analysis. *Id.*

58. *See id.* at 553-54.

59. *Id.* at 554.

60. The court's discussion is puzzling for another reason. In describing the analysis to be undertaken, the court stated: "The question is whether the probative value of the photograph outweighed its prejudicial effect." *Id.* at 553 (citing Isaacs v. State, 659 N.E.2d 1036, 1043 (Ind. 1995)). This statement seems to stand Rule 403 on its head: Under Rule 403, evidence should only be excluded if its probative value *is substantially outweighed by* its prejudicial effect. *See* Ind. R. Evid. 403. The court's formulation may not be entirely inconsistent with Rule 403, but it raises the possibility of unnecessary confusion.

61. 696 N.E.2d 386 (Ind. 1998).

photograph represented cumulative evidence on the point for which it was offered. *Young* was a murder prosecution in which the murder victim's two young children were found at the scene, each of them injured and covered in blood.[62] At trial, the prosecution offered a photograph of one of the children, taken at the crime scene, to illustrate testimony concerning the child's injuries. On appeal, the supreme court acknowledged that the photograph was cumulative evidence, but concluded, again without discussing the precise nature of the photograph, that the photograph was not "so prejudicial as to improperly influence the jury."[63]

Robinson and *Young* suggest that the Indiana Supreme Court is receptive to the use of photographs of crime victims, even where the probative value of the photographs is minimal (because the photographs are cumulative of other evidence) and the photographs' content is admittedly gruesome and therefore likely to incite an emotional response in the jury. The court's analysis may appear to give short shrift to Rule 403. It is not, however, entirely inconsistent with the approach taken by other courts.[64]

B. Character of the Victim

Rule 404(a) provides that evidence of character is not admissible to prove action in conformity with that character, except in three instances.[65] First, an accused may offer evidence of a pertinent trait of his character; if he does so, the prosecution may offer character evidence in rebuttal.[66] Second, an accused may offer evidence of a pertinent character trait of a victim. The prosecution may again offer evidence of the victim's character in rebuttal; in addition, if the accused in a homicide prosecution asserts self-defense and claims that the victim was the first aggressor, the prosecution is entitled to introduce evidence of the victim's character for peacefulness.[67] Finally, evidence of the character of a witness may be admitted in accordance with Rules 607, 608, and 609.[68] Character is to be demonstrated by opinion or reputation testimony; only on cross-examination is inquiry into specific instances of conduct permitted, unless character forms an essential element of a charge, claim, or defense.[69]

In *Coleman v. State*,[70] a case decided under the common-law scheme that predated the adoption of the Rules, the Indiana Supreme Court noted that, where

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62. *Id.* at 388.

63. *Id.* at 389.

64. *Cf.* United States v. Hall, 152 F.3d 381, 400-02 (5th Cir. 1998) (allowing photographs of murder victim's exhumed body, in a state of decomposition, admissible as evidence of the victim's identity and cause of death, despite the defendant's willingness to stipulate to same).

65. IND. R. EVID. 404(a).

66. IND. R. EVID. 404(a)(1).

67. IND. R. EVID. 404(a)(2).

68. IND. R. EVID. 404(a)(3).

69. IND. R. EVID. 405.

70. 694 N.E.2d 269 (Ind. 1998).

a defendant asserts self-defense, evidence of the victim's violent character may be admitted under either of two theories: First, to show that the victim had a violent character and that the defendant therefore had reason for fear; or, second, to show that the victim initiated the violent incident for which the defendant is charged.[71] On the first theory, evidence of prior acts of violence is admissible, provided the defendant can show that she was aware of the prior acts; on the second theory, however, only reputation evidence is admissible.[72] The defendant here had attempted to show that she feared the victim, and in support of her claim had offered evidence that she had seen the victim carrying a gun on several occasions. Because this evidence was offered to show that the defendant feared the victim, and not simply to show that the victim was a violent man, the supreme court held that the evidence should have been admitted.[73]

The distinction drawn in *Coleman* is solidly grounded in the difference between the two theories. Where the defendant's claim is that she had reason to fear the victim, the issue is her state of mind rather than simply the victim's character, and specific acts known by the defendant can properly have as great an impact, if not greater, on that state of mind as can the defendant's knowledge of the victim's reputation within the community. In contrast, use of specific acts as proof of character, to show action in conformity with that character, would require a two-step inference that would focus the jury's attention, not on conduct on the occasion in question, but on conduct on other occasions, and would create the danger of a jury deciding the case based on its judgment of the conduct on the other occasions. This double inference was prohibited at common law, and is forbidden under the Rules.[74] Thus, while *Coleman* was decided under the common law, the same result should obtain under the Rules.

C. *Other Acts*

Rule 404(b) provides that evidence of other acts by the defendant are not admissible to prove character, in order to prove action in conformity therewith.[75] The Rule states, however, that evidence of other acts may be admissible for other purposes; the Rule then sets forth a non-exclusive list of permissible purposes for which other act evidence may be admitted, including "proof of motive, intent, preparation, plan, knowledge, identity, or absence of mistake or accident."[76] Rule 404(b) creates difficulties in practice, because of the very real danger that, presented with evidence of unsavory acts by the defendant, the jury will, despite contrary instructions, leap to the forbidden inference that, because the defendant

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71. *Id.* at 277 (quoting Phillips v. State, 550 N.E.2d 1290, 1297 (Ind. 1990)).

72. *See id.*

73. *Id.* The court further held, however, that the trial court's error was harmless, because the defendant had been allowed to introduce substantial other evidence to establish her fear of the victim. *Id.*

74. IND. R. EVID. 405.

75. IND. R. EVID. 404(b).

76. *Id.*

engaged in the other acts, he must be a bad person, and because he is a bad person, he must have committed the crime with which he is charged. Since the adoption of the Indiana Rules of Evidence, Rule 404(b) has consistently proved one of the most troublesome in operation, and this year was no different.

In *Hicks v. State*,[77] the Indiana Supreme Court adopted a two-part test for the application of Rule 404(b): First, "the court must determine that the evidence of other crimes, wrongs, or acts is relevant to a matter at issue other than the defendant's propensity to commit the charged act," and second, "the court must balance the probative value of the evidence against its prejudicial effect pursuant to Rule 403."[78] Cases decided during the survey period raised questions under both prongs of the *Hicks* test.

1. Motive.—*Hicks* itself involved a claim that prior acts of violence between the defendant and the victim constituted evidence of motive for murder and therefore were not barred by Rule 404(b). In *McEwan v. State*,[79] the court relied upon *Hicks* in holding that evidence of a prior fight between the defendant and his girlfriend (the victim of the murder for which the defendant was being prosecuted) was relevant to show the defendant's hostility toward the victim, which constituted the "paradigmatic motive" for murder.[80]

2. Plan.—In *Giles v. State*,[81] the Indiana Court of Appeals analyzed the circumstances in which evidence of other acts may properly be admitted as evidence of a plan. In *Giles*, the defendant was charged with theft after cashing a bad check, payable to himself, styled as a payroll check, and drawn on an account that the defendant had created for a company he controlled. At trial, the prosecution offered evidence that, during the month the defendant allegedly cashed the bad check that formed the subject of the charge, he cashed fourteen other bad checks from the same account, each of which shared essential characteristics of the check that formed the subject of the charge.[82] In concluding that the other fourteen checks were admissible as evidence of a plan, the court drew on pre-Rules precedent, requiring that the other acts "be so related in character, time and place of commission as to establish some plan which embraced both the prior and subsequent criminal activity and the charged crime."[83]

3. Other Purposes.—It bears repeating that the examples listed in Rule 404(b) of purposes for which other acts evidence may be admitted are not

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77. 690 N.E.2d 215 (Ind. 1997).

78. *Id.* at 221. Although *Hicks* was decided within this year's survey period, it received extensive treatment in last year's survey article. *See* Sean P. O'Brien, *Survey of Recent Developments in Indiana Evidence Law*, 31 IND. L. REV. 589, 597-99 (1998). The author of this year's survey agrees with Mr. O'Brien's conclusion that some aspects of *Hicks* are problematic. In the interest of avoiding duplication, the reader is referred to Mr. O'Brien's article. *Id.*

79. 695 N.E.2d 79 (Ind. 1998).

80. *Id.* at 87-88.

81. 699 N.E.2d 294 (Ind. Ct. App. 1998).

82. *See id.* at 299.

83. *Id.* at 299-300 (citing Lannan v. State, 600 N.E.2d 1334, 1339 (Ind. 1992)).

exclusive. In *Parmley v. State*,[84] the Indiana Court of Appeals approved the admission of evidence of other acts by the defendant to explain actions by the victim, as a means of rebutting the defendant's attack on the victim's credibility. In *Parmley*, a child molestation case, the trial court admitted evidence that the defendant threatened and beat his wife and children, and that the defendant engaged in cross-dressing, bondage, and homosexual acts. The court of appeals concluded that, in light of the defendant's charge that the victim fabricated her allegations and was being improperly influenced by her mother, this evidence was properly admitted to explain, first, why the victim (the defendant's daughter) did not immediately raise her allegations of sexual abuse, and, second, why she had left her father's home for her mother's.[85]

4. Weighing Probative Value Against Prejudicial Effect.—Pursuant to *Hicks*, the Indiana courts are expressly directed to engage in Rule 403 balancing of probative value against the danger of unfair prejudicial effect in situations where the admission of other acts evidence is sought. Of course, Rule 403 problems may arise with regard to virtually any kind of evidence, but problems are particularly likely to occur when evidence of other acts is offered under Rule 404(b), because of the lure of the forbidden inference.[86] This likelihood requires that courts take seriously their obligation to engage in careful balancing, to ensure that evidence of other acts is not admitted in situations in which the danger of unfair prejudice substantially outweighs the evidence's probative value.

On at least one occasion during the survey period, the Indiana Court of Appeals failed to meet its obligation. In *Parmley*, it will be recalled, the court affirmed the trial court's decision to admit evidence that the defendant threatened and beat his wife and children and that he engaged in acts of cross-dressing, bondage, and homosexuality. Having concluded that this evidence was relevant for a purpose other than as evidence of character,[87] the court dismissed the Rule 403 argument out of hand, concluding that although the evidence might have been prejudicial, the prejudice was not unfair, and that even if it were, the unfair prejudice did not substantially outweigh the probative value of the evidence.[88]

The *Parmley* court's analysis threatens to reduce Rule 403 to meaninglessness. The introduction of evidence of the defendant's prior acts of violence and unusual sexual proclivities, in a case involving an allegation of child molestation, raises a clear danger that the jury, outraged by the evidence of other acts, will conclude that the defendant is a vile individual who is likely to have committed the charged offense.[89] This is precisely the line of reasoning that

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84. 699 N.E.2d 288 (Ind. Ct. App. 1998).

85. *Id.* at 293-94.

86. *See supra* note 76 and accompanying text.

87. *See supra* notes 84-85 and accompanying text.

88. *Parmley*, 699 N.E.2d at 294.

89. I wish to make clear that I do not in any way regard homosexuality, or engaging in homosexual acts, as evidence of "vile" character. The evidence presented against the defendant included evidence of unusual sexual practices that might easily have some tendency to incite disgust

Rule 404(b) prohibits. In light of this obvious danger, the *Parmley* court's conclusion that any prejudice to the defendant was not unfair is simply indefensible. This is particularly so because the *Parmley* decision does not note what limiting instructions, if any, the jury received regarding the evidence of the defendant's acts of violence and unusual sexual behavior. The absence of a strong limiting instruction would dramatically increase the likelihood that the jury would leap to the forbidden inference. It might be that, after engaging in a careful balancing of probative value against unfair prejudicial effect, and taking into account the limiting instructions, if any, that the jury received, a court could conclude in a review of *Parmley* that the danger of unfair prejudicial effect did not substantially outweigh the probative value of the other acts evidence, or that the trial court did not abuse its discretion in reaching such a conclusion. The decision in *Parmley*, however, reduced the Rule 403 analysis to a sham.

D. Habit and Routine Practice

Rule 406 provides that evidence of habit or routine practice is admissible to show that action on a particular occasion conformed with the habit or routine practice.[90] The theory underlying the admission of evidence of habit or routine practice is that when an individual repeatedly confronts a particular set of circumstances and responds to those circumstances in the same way, at some point the individual's response becomes virtually automatic. Because conscious thought is removed from the picture, it becomes reasonable to infer that on subsequent occasions in confronting the same situation, the individual responded in the same virtually automatic way. Evidence of habit and routine practice, which is admissible to prove action in conformity therewith, is distinguished from character, which is not admissible to prove action in conformity therewith, by both the specificity of the situations in which the habit comes into play and the specificity of the reaction to the particular situation. Thus, "John is a careful driver" is evidence of character, while "John always comes to a full stop at the corner of Nineteenth and Elm" is evidence of habit. The Indiana Court of Appeals, however, has cautioned against too narrow a reading of the situational prerequisite for evidence of habit or routine practice.

In *Fitch v. Maesch*,[91] the court considered a contest to the probate of a will. At issue was whether the will had been properly executed. Only one of the witnesses to the execution remained alive at the time of the challenge, and she did not recall the specifics of the execution. The proponent of the will therefore offered the testimony of the secretary for the lawyer who prepared the will and supervised its execution. The secretary testified to the lawyer's normal practice in supervising the execution of wills, and further stated that she could not recall a single instance in which the lawyer had departed from his standard practice.[92]

in the jury.

90. IND. R. EVID. 406.

91. 690 N.E.2d 350 (Ind. Ct. App. 1998).

92. *See id.* at 353. The secretary established a foundation for her testimony regarding the

The plaintiff objected that this testimony did not establish a habit or routine practice that was relevant to the case at hand, because the secretary's testimony only established the lawyer's habit or routine practice in circumstances in which the secretary served as a witness. The court of appeals rejected this argument, concluding that it was proper to consider the evidence as tending to establish a habit or routine practice with respect to the execution of wills generally, and not solely to the execution of wills on occasions in which the secretary was present.[93]

E. Offer of Settlement

Under Rule 408, statements made during settlement negotiations, including offers of settlement, are inadmissible to establish either liability or a claim's lack of merit.[94] The Rule leaves open the possibility, however, that statements made during settlement negotiations may be admissible for other purposes. This point was brought home by the Indiana Court of Appeals' decision in *Vernon v. Acton.*[95] In that case, a negligence action arising out of an automobile accident, the defendants asserted as a defense that the plaintiffs had agreed to a settlement in a mediation that preceded the filing of the complaint. In support of their contention, the defendants offered testimony of the mediator and of the claims representative for the defendants' insurance company that the plaintiffs had agreed to settle their claims, although the agreement had not been reduced to writing and signed by the parties.[96] The plaintiffs objected that this evidence violated Rule 408, but the court of appeals disagreed. The court concluded that the evidence was not being offered on the merits of the underlying negligence claim, but rather to show that a settlement had been reached—an issue unrelated to the merits—and was therefore admissible.[97]

III. PRIVILEGES

Like the Federal Rules of Evidence, the Indiana Rules of Evidence do not themselves establish evidentiary privileges. And like Federal Rule of Evidence 501, which calls on the federal courts, in suits arising under federal law, to develop a common law of privileges based on the dictates of experience and reason,[98] Indiana's Rule 501 permits the evolution of privileges through the

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lawyer's habit by testifying that she had worked for the lawyer for sixteen years, had typed wills almost every day during that period, and had witnessed the execution of more than five hundred wills with the lawyer. *See id.*

93. *Id.*

94. IND. R. EVID. 408.

95. 693 N.E.2d 1345 (Ind. Ct. App. 1998).

96. *See id.* at 1348.

97. *Id.* at 1348-49. The court also noted that Indiana Rule of Alternative Dispute Resolution 2.11, which protects the confidentiality of the mediation proceeding, did not apply, because the mediation did not take place within the context of ongoing litigation but rather preceded the filing of the complaint. *Id.* at 1348.

98. FED. R. EVID. 501.

common law.[99] The courts have been reluctant, however, to draw on common-law principles in developing the law of evidentiary privileges. Instead, the courts have followed a path of strict construction of statutorily-created privileges, and have declined to recognize additional privileges, even in those circumstances in which the courts have concluded that public policy concerns support the recognition of a privilege.[100]

A. Physician-Patient Privilege

The Indiana Code creates a privilege protecting communications by patients to physicians in the course of professional business and advice given in the course of such business.[101] In *Ley v. Blose*,[102] the Indiana Court of Appeals construed this privilege narrowly, concluding that normally the privilege applied only to physicians and not to hospitals or other medical facilities.[103] As a result, the privilege did not protect a patient's medical records that were maintained by a hospital or other medical facility, rather than personally by a doctor.[104]

The result reached in *Ley* suggests an overly strict approach to the interpretation of statutory privileges that yields arbitrary results and threatens to undermine the rationale behind the privileges. Making the privileged status of communications set forth in medical records turn on the fortuity of whether a doctor maintains her own patient records within her own office, or relies on hospital personnel to do so, bases the privilege on a factor that will hardly occur to most patients seeking medical treatment. Moreover, the approach taken in *Ley* seems contrary to the general principle that the privilege belongs to the patient, not to the physician, and that therefore only the patient can effectively waive the privilege. Under that principle, even if the maintenance of patient records by a hospital represented disclosure by the physician to third parties who were not themselves within the statutory privilege, the privilege should remain in effect, provided that the patient herself does not disclose the confidential communications.

Most jurisdictions that recognize the physician-patient privilege extend the privilege to medical records maintained by hospitals or other medical facilities, at least insofar as those records contain communications between patients and physicians.[105] It may be, in these jurisdictions, that some records that do not

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99. IND. R. EVID. 501(a).

100. *See* Deasy-Leas v. Leas, 693 N.E.2d 90, 99 (Ind. Ct. App. 1998), discussed *infra* at notes 109-18 and accompanying text.

101. IND. CODE § 34-46-3-1(2) (1998).

102. 698 N.E.2d 381 (Ind. Ct. App. 1998).

103. *Id.* at 383.

104. *See id.* at 383 & n.2.

105. *See, e.g.*, State v. Henneberry, 558 N.W.2d 708, 709 (Iowa 1997); State v. McElroy, 553 So. 2d 456, 459-60 (La. 1989); State *ex rel.* Jones v. Syler, 936 S.W.2d 805, 807 (Mo. 1997) (en banc); People v. Carkner, 623 N.Y.S.2d 350, 353-54, *app. denied*, 629 N.Y.S.2d 730 (1995); Prince v. Duke Univ., 392 S.E.2d 388, 390 (N.C. 1990); Shamburger v. Behrens, 380 N.W.2d 659,

contain such communications will fall outside the privilege.[106] The distinction there seems to rest, however, on the contents of the particular records at issue, not on the location in which those records are maintained. Given the arbitrary result approved in *Ley* and the questionable rationale underlying that result, the scope of the patient-physician privilege merits reconsideration by future courts confronted with the issue.

B. Patient-Psychotherapist Privilege

The Indiana Code also recognizes a privilege for patient-psychotherapist communication. In *Kavanaugh v. State*,[107] the Indiana Court of Appeals emphasized that the privilege only protects statements made in a therapeutic setting. In *Kavanaugh*, a prosecution for child molesting, the prosecutor sought to introduce testimony from the defendant's therapist concerning admissions that the defendant made in a meeting with the therapist, the defendant's lawyer, and the mother of the victim. The court noted that the meeting "was conducted for non-therapeutic reasons, outside the scope of a normal therapist-client relationship," and that statements by the defendant within the meeting therefore were not protected by the patient-psychotherapist privilege.[108]

C. No Privilege for Communications Between Child and Guardian ad Litem

In *Deasy-Leas v. Leas*,[109] a child custody proceeding, the guardian ad litem sought to quash a discovery request that would have required him to turn over his file relating to the child. On interlocutory appeal, the court of appeals considered whether a privilege existed to protect communications between a guardian ad litem and the child whose interests the guardian ad litem was appointed to protect. As a starting point, the court noted that there was no statutory privilege for communications between guardians ad litem and their wards, and that the court itself lacked the authority to create such a privilege.[110] Despite the absence

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662 (S.D. 1986).

106. *See McElroy*, 553 So. 2d at 459-60; *Carkner*, 623 N.Y.S.2d at 353-54; *Prince*, 392 S.E.2d at 390.

107. 695 N.E.2d 629 (Ind. Ct. App. 1998).

108. *Id.* at 631.

109. 693 N.E.2d 90 (Ind. Ct. App. 1998).

110. *Id.* at 94-95. As a preliminary matter, the court noted that a recently-passed statute provided that when a guardian ad litem was appointed to perform an investigation and prepare a report for the court, the report must be made available to other parties to the custody proceeding. *See* IND. CODE § 31-17-2-12 (1998). The court concluded that this provision was inapplicable to the case before it because it did not appear that the guardian ad litem in the case had been appointed to perform an investigation and prepare a report, nor was it apparent that the other statutory prerequisites had been met. *Deasy-Leas*, 693 N.E.2d at 93-94. Because the statute that expressly provided for disclosure was not applicable, the court found it necessary to consider more broadly the question of whether a privilege or other protections barred or limited the disclosure sought in the case before it.

of an express privilege, the court found some indication that the legislature meant certain communications by and about children to be afforded some level of confidentiality. For example, the custody statutes allow a court to prevent the record of any interview, report, or investigation from becoming part of the public record if the court deemed such protection in the best interest of the child.[111] Rule 26 of the Indiana Rules of Trial Procedure similarly provide for the possibility of protective orders "to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense."[112] Finally, certain communications are subject to recognized privileges, including communications between a student and a school counselor.[113] These provisions and others create what the court called a "specter of confidentiality" surrounding materials contained in a guardian ad litem's file.[114] Despite its apparent conviction that public policy reasons favored at least a limited privilege, however, the court declined to recognize such a privilege in the absence of a statutory command. Any protection would have to come from the general confidentiality provisions of the custody statutes and Indiana Trial Rule 26(c).[115]

The court's reluctance to recognize a privilege protecting communications between a guardian ad litem and his charge is certainly understandable, given the small number of jurisdictions that recognize such a privilege and the uncertainties surrounding the role of the guardian ad litem in protecting the best interests of the child.[116] Privileges obscure the pursuit of truth at trial by keeping relevant and otherwise admissible evidence from the factfinder; thus, courts generally tend to read privileges narrowly, to confine them within the bounds of their underlying rationales, and are wary when pressed to recognize new privileges. Yet the court's absolutist position that it lacked the authority to recognize a privilege in the absence of a statutory mandate appears inconsistent the Rules, which recognize the possibility of privileges created "by principles of common law in light of reason and experience."[117] The *Deasy-Leas* court relied on pre-Rules caselaw for the proposition that it lacked authority to find privileges that were not embodied in statutory law;[118] in light of the plain text of Rule 501(a), that reliance seems unwarranted.

D. No Qualified Privilege for the Press

Privileges may of course be based on constitutional provisions, as well as statutes, rules, and common law decisions. The privilege against self-

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111. IND. CODE § 31-17-2-2 (1998).

112. IND. R. TRIAL P. 26(c).

113. IND. CODE § 20-6.1-6-15 (1998).

114. *Deasy-Leas*, 693 N.E.2d at 97.

115. *See id.* at 99.

116. *Id.* at 94, 98.

117. IND. R. EVID. 501(a).

118. *Deasy-Leas*, 693 N.E.2d at 94-95 (citing Scroggins v. Uniden Corp. of Am., 506 N.E.2d 83, 85 (Ind. Ct. App. 1987)).

incrimination under the Fifth Amendment of the United States Constitution is perhaps the most obvious example. The news media, for years, has argued that the First Amendment creates a privilege for news gatherers, and some federal courts of appeals have accepted their contentions.[119] The Indiana Supreme Court, however, has declined to follow their lead. In *In re WTHR-TV*,[120] the court was asked to accept a qualified reporter's privilege that would protect information gathered by reporters from disclosure unless "(1) the information is 'clearly material and relevant' to the party's claim or defense; (2) the information is 'critical to the fair determination of the cause'; and (3) the party has 'exhausted all other sources for the same information.'"[121] Rather than rely on the federal appellate decisions that had recognized the proposed privilege, the court turned to *Branzburg v. Hayes*,[122] in which the U.S. Supreme Court held that the First Amendment did not create a qualified privilege that would allow a reporter to withhold the identity of sources from a grand jury. The *WTHR* court noted that the three-part test for a qualified privilege proposed by the station had been set forth in the dissent in *Branzburg*. The court thus declined to read *Branzburg* as requiring a test that the *Branzburg* majority itself rejected.

The supreme court's rejection of the three-part test was unnecessary for its resolution of the case because the court concluded that even if the privilege existed in the abstract, it would not apply to the facts of the case before it.[123] Nevertheless, given the force with which the court stated its rejection of the First Amendment privilege, the issue may be regarded as settled, at least as a practical matter, for the foreseeable future.

IV. IMPEACHMENT

A. *Vouching*

Though not expressly stated in any of the Rules of Evidence, Indiana law has long held that the government may not expressly vouch for the credibility of its witnesses in a criminal prosecution. In *Bouye v. State*,[124] the Indiana Supreme Court reasserted this general rule, although its application to the case at hand was curious. *Bouye* was a prosecution for murder, conspiracy to commit robbery, and carrying a handgun without a license. Bouye's co-defendant accepted a plea and

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119. *See, e.g.*, Shoen v. Shoen, 5 F.3d 1289, 1292-93 (9th Cir. 1993); United States v. Burke, 700 F.2d 70, 76-77 (2d Cir. 1983).

120. 693 N.E.2d 1 (Ind. 1998).

121. *Id.* at 10.

122. 408 U.S. 665 (1972).

123. *In re WTHR-TV*, 693 N.E.2d at 15. In *WTHR*, a defendant in a murder prosecution sought to compel the television station to turn over unedited tapes of an interview the station had conducted with her. The court concluded that under these circumstances, disclosure did not threaten to chill news gathering and the use of confidential sources because the individual seeking the disclosure was herself the source of the materials the disclosure of which she sought. *Id.* at 13.

124. 699 N.E.2d 620 (Ind. 1998).

agreed to testify against Bouye at trial. On cross-examination, Bouye's counsel asked whether the terms of the plea agreement required that the witness's testimony be truthful. In voicing his objection, the prosecutor stated: "There's no question about the fact that he's required to testify truthfully. If he does not then I certainly will move the Court to set aside the plea agreement and that he be tried. . . . I certainly wouldn't ask a witness to tell anything but the truth."[125] On defense counsel's objection to this commentary, the court admonished the jury that the word "truthfully" did not appear in the plea agreement and that the jury must disregard any statements to the contrary.[126] Bouye was then convicted.

On appeal, Bouye argued that the prosecutor's statement constituted improper vouching for the prosecutor's witness. The supreme court rejected the argument, concluding that the prosecutor's comments were prompted by the cross-examination and represented only a general assertion that the government would not ask any witness to lie, with no mention of the particular witness who was testifying.[127] The court's conclusion is a bit confusing because the prosecutor's comments, taken as a whole, certainly mentioned the particular witness. The general comment, taken in conjunction with the statements concerning the particular witness, easily could be read as an assertion that the government would not ask this particular witness to lie. The court thus seems to take an extremely narrow approach to improper vouching.

B. Impeachment by a Prior Conviction—Rule 609(b)

Rule 609 allows prior convictions for enumerated crimes to be used for impeachment purposes.[128] Rule 609(b) limits the use of stale convictions, requiring that when the prosecution wishes to impeach a criminal defendant with a conviction that is more than ten years old, the prosecution must provide advance written notice of the prosecution's intent to use the conviction; in addition, the prosecution must convince the judge that the probative value of the stale conviction substantially outweighs its prejudicial effect.[129]

In *Giles v. State*,[130] the court of appeals addressed the scope and purpose of Rule 609(b)'s requirement of advance notice. In *Giles*, the state sought to impeach the defendant with a twenty-year-old conviction for uttering a forged

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125. *Id.* at 622.

126. *See id.* at 623.

127. *Id.* at 625.

128. Rule 609(a) provides that a witness may be impeached through evidence of conviction for "murder, treason, rape, robbery, kidnapping, burglary, arson, criminal confinement or perjury," or any "crime involving dishonesty or false statement." IND. R. EVID. 609(a). In its enumeration of crimes, the Indiana Rule differs from the Federal Rule, which allows impeachment not only through evidence of conviction for crimes involving dishonesty or false statement but also through evidence of conviction for any crime "punishable by death or imprisonment in excess of one year." FED. R. EVID. 609(a).

129. IND. R. EVID. 609(b).

130. 699 N.E.2d 294 (Ind. Ct. App. 1998).

instrument. It was undisputed that the state failed to provide advance written notice of its intent to use this conviction.[131] The state contended, however, that its filing of an habitual offender charge, which included the stale conviction, provided the defendant with adequate actual notice. The court of appeals disagreed. Drawing on the commentary to Rule 609(b), the court suggested that the notice required by Rule 609(b) should include four elements: the date of the conviction, the jurisdiction in which the conviction occurred, the offense, and the "specific facts and circumstances" on which the prosecution relies to justify admission.[132] The purpose for this last requirement, the court concluded, was not simply to put the defendant on notice of the existence of the older conviction (about which the defendant was presumably aware even in the absence of notice), but to allow the defendant the opportunity to prepare to meet the prosecution's arguments concerning probative value and prejudicial effect. Because the habitual offender charge did not provide the defendant with the required notice of the facts and circumstances on which the prosecution intended to rely in support of admission, the prior conviction was improperly admitted.[133]

In reaching this conclusion, the court disagreed with *United States v. Sloman*,[134] in which the Sixth Circuit, interpreting the parallel provision in the Federal Rules of Evidence, concluded that any failure to provide advance notice was harmless error if the defense counsel knew of the stale conviction. The *Giles* court argued that the Sixth Circuit misunderstood the surprise that the required advance notice was intended to prevent: "[T]he surprise to be avoided is the surprise associated with being unprepared to argue probative value and prejudicial effect, not surprise associated with mere knowledge of the conviction."[135]

C. Cross-examination

It is axiomatic that the use of leading questions is, in most instances, an appropriate method of cross-examination, and Rule 611(c) so states.[136] Interesting issues arise, however, where the witness being cross-examined is the lawyer's own client, called as a hostile witness by the other side. In such situations, cross-examination by leading questions raises the unseemly image of "the client . . . parroting words put in his mouth by his lawyer."[137] The Advisory

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131. *See id.* at 297.

132. *Id.*

133. *See id.* The court further noted that the prosecution had failed to make the required showing that the probative value of the conviction substantially outweighed its prejudicial effect, and the trial court had failed to engage in the required balancing of probative value against prejudicial effect before admitting the conviction. *Id.* at 298.

134. 909 F.2d 176 (6th Cir. 1990).

135. *Giles*, 699 N.E.2d at 297 n.3.

136. IND. R. EVID. 611(c).

137. William F. Harvey, *Rules of Procedure Annotated*, 3 IND. PRACTICE § 43.3, at 205 (2d ed. 1988).

Committee note on Federal Rule of Evidence 611(c), recognizing the problem, suggests that cross-examination by leading questions is inappropriate "when the cross-examination is cross-examination in form only and not in fact, as for example the 'cross-examination' of a party by his own counsel after being called by the opponent."[138]

In *Bonadies v. Sisk*,[139] however, the court of appeals concluded that Rule 611(c) does not automatically bar cross-examination of a party by the party's lawyer. Although the court acknowledged the potential difficulties posed by a lawyer leading her own client, it noted that Indiana's Trial Rule 43 expressly contemplated that where one party calls a hostile witness, the other side may cross-examine by leading questions.[140] Ultimately, the court concluded, the trial court has the power, in the exercise of its discretion, to regulate the scope, method, and manner of cross-examination. Because the cross-examination here remained within the scope of the direct examination, the trial court did not abuse its discretion.[141]

V. Expert Witnesses

In the 1993 case of *Daubert v. Merrell Dow Pharmaceuticals*,[142] the United States Supreme Court addressed the standards, under Federal Rule of Evidence 702, for the admission of expert scientific testimony. The *Daubert* decision emphasized the importance of the trial court's role as gatekeeper in ensuring the reliability and relevance of scientific evidence placed before the jury. In performing this function, the trial court may consider any number of factors that bear on reliability; among these factors, in appropriate cases, are (1) whether the theory or technique underlying the expert's testimony has been tested, (2) whether the theory or technique has undergone peer review and publication, (3) whether the theory or technique yields a known or potential rate of error, and (4) whether the theory or technique is generally accepted within the pertinent scientific community.[143] The *Daubert* decision has significantly altered the analysis that federal courts perform in deciding whether to admit expert scientific testimony. *Daubert* did, however, leave some questions unanswered, among them: (1) how is the court to distinguish scientific testimony from testimony that simply draws on "technical, or other specialized knowledge"; (2) of what significance (if any) is the distinction;[144] and (3) in assessing reliability, to what extent may the court look beyond the methods used by the expert and evaluate

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138. Fed. R. Evid. 611, note c.

139. 691 N.E.2d 1279 (Ind. Ct. App. 1998).

140. *Id.* at 1281.

141. *See id.* at 1282.

142. 509 U.S. 579 (1993).

143. *See id.* at 593-94.

144. The U.S. Supreme Court has granted *certiorari* in a case that raises these first two issues. *See* Carmichael v. Samyang Tire Co., 131 F.3d 1433 (11th Cir. 1997), *cert. granted*, 118 S. Ct. 2339 (1998).

the reliability of the conclusions derived from the application of those methods?[145]

The Indiana Court of Appeals addressed this last question in *Lytle v. Ford Motor Co.*[146] *Lytle* arose out of an accident in which a woman was thrown from the pickup truck in which she was riding; she sustained serious head injuries as a result. The plaintiffs claimed that the injuries suffered in the accident were exacerbated by the failure of the injured woman's seatbelt. In support of this claim, the plaintiffs sought to present the expert testimony of two engineers, who would testify that the seatbelt released either inertially or through inadvertent contact, and that the seatbelt's failure under these circumstances constituted a design defect.[147] The trial court refused to allow either expert to testify, and the court of appeals affirmed.

As to the first expert, the court of appeals concluded that his testimony regarding inadvertent release did not rest on scientific principles, and thus did not invoke the explicit reliability requirement of Rule 702(b).[148] The court nevertheless determined that the expert had failed to perform sufficient tests to support his conclusion, and that the trial court therefore had not abused its discretion by barring the expert's testimony.[149] The first expert's testimony about inertial release likewise was flawed, according to the court: Although this testimony did involve scientific principles, the expert relied on a testing method that both government regulators and the Society of Automotive Engineers had rejected. The testimony therefore was properly excluded as unreliable.[150]

The court of appeals' discussion of the second expert's testimony, however, raises some difficult issues. In analyzing the admissibility of the expert's testimony, the court assessed not only the reliability of the expert's methods but also the reliability, according to scientific principles, of the expert's conclusions. The legal analysis undertaken by the court is consistent with the United States Supreme Court's approach to Federal Rule 702. Although the *Daubert* Court stated that the trial court's "focus . . . must be solely on principles and methodology, not on the conclusions that they generate,"[151] the Court later qualified its seemingly unequivocal statement:

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145. Indiana's courts, when addressing problems under the Indiana Rules of Evidence, are of course not bound by decisions of the Federal courts interpreting the parallel Federal Rules. And unlike the Federal Rule, Indiana's Rule 702 by its terms calls upon the trial judge to admit expert scientific testimony "only if the court is satisfied that the scientific principles upon which the expert testimony rests are reliable." Ind. R. Evid. 702(b). Nevertheless, the Indiana Supreme Court, while declining to adopt the *Daubert* test expressly, has stated repeatedly that the Indiana courts should be guided by *Daubert* in their application of Rule 702(b). *See* Steward v. State, 652 N.E.2d 490, 498 (Ind. 1995).

146. 696 N.E.2d 465 (Ind. Ct. App. 1998).

147. *See id.* at 467-68.

148. *Id.* at 470.

149. *Id.* at 470-71.

150. *See id.* at 471.

151. *See* Daubert v. Merrell Dow Pharm., 509 U.S. 579, 595 (1993).

> But conclusions and methodology are not entirely distinct from one another. Trained experts commonly extrapolate from existing data. But nothing in either *Daubert* nor in the Federal Rules of Evidence requires a district court to admit opinion evidence which is connected to existing data only by the *ipse dixit* of the expert. A court may conclude that there is simply too great an analytical gap between the data and the opinion proffered.[152]

Under *Daubert* and its progeny (and bearing in mind the Indiana courts' qualified acceptance of the *Daubert* framework), therefore, it was proper for the *Lytle* court to analyze the scientific soundness of the expert's conclusions as well as his methodology.[153]

In undertaking this analysis, however, a court must take care not to intrude on the jury's role in weighing competing evidence and assessing the credibility of witnesses, an intrusion that is more likely when the soundness of conclusions is assessed than it is when only methodology is at issue. In *Lytle*, the court of appeals accepted that the second expert's methods were reliable; it questioned only whether the results of the expert's tests supported his conclusions. In affirming the trial court's rejection of the plaintiff's expert's conclusions, the court relied principally on evidence presented by the defendant, including tests performed by the defendant's own experts. The circumstances thus resembled the battle of experts before the jury that typically lies at the heart of a design defect case. As Judge Riley noted in her concurring and dissenting opinion in *Lytle*, the trial court's gatekeeping function under *Daubert* is not meant to usurp the function of the jury in weighing competing evidence presented through the adversary system.[154] Yet the majority concluded that the plaintiff's expert's testimony was properly kept from a jury.[155] The majority's decision in *Lytle* arguably was defensible, because the plaintiff's expert's opinion not only was contrary to the evidence submitted by the defendant's experts but also was inconsistent with results reached separately by the National Highway Traffic Safety Administration and the Society of Automotive Engineers.[156] Still, courts should be wary of a broad reading of *Lytle*, lest they inappropriately invade the jury's province.

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152. General Elec. Co. v. Joiner, 118 S. Ct. 512, 519 (1997).

153. Judge Riley, concurring in part and dissenting in part in *Lytle*, cited only the *Daubert* Court's unqualified statement that the focus should be only on methodology, not conclusions; she did not take note of the U.S. Supreme Court's subsequent decision in *Joiner*. *See Lytle*, 696 N.E.2d at 474-75 (Riley, J., concurring in part and dissenting in part).

154. *See Lytle*, 696 N.E.2d at 475 (Riley, J., concurring in part and dissenting in part) (citing United States v. 14.38 Acres of Land, 80 F.3d 1074, 1078 (5th Cir. 1996)).

155. *Id.* at 474.

156. *See id.* at 472.

VI. Hearsay

A. Purpose: Truth of the Matter Asserted

Fundamental to the hearsay rules is the principle that a statement is only considered hearsay if it is being offered to prove the truth of the matter asserted.[157] If the purpose for which the statement is offered does not depend on the statement's truth, the hearsay bar does not apply.

A case perhaps more remarkable for its long and tangled history than for its final result illustrates the need for care when a judge assesses a claim that an out-of-court statement is being offered for a purpose other than its truth. *Mason v. State*[158] was a second direct appeal, following a first, unsuccessful direct appeal,[159] an unsuccessful petition for post-conviction relief,[160] and a successful habeas corpus petition in federal court.[161] At the trial in *Mason*, the prosecution presented the testimony of a police witness, who on two occasions informed the jury, over the defendant's hearsay objection, of the content of an informant's tip that led the police to investigate the defendant.[162] The defendant contended that this testimony constituted impermissible hearsay. The prosecution countered that the testimony was properly offered, not to establish the truth of what the informant said, but to explain why the police launched their investigation of the defendant. On the second direct appeal, the supreme court rejected the prosecution's argument concluding that the reasons for the police investigation were not a proper issue in the case and that, in any event, the jury had not received an instruction that it was not to consider the informant's statement for its truth.[163] In the absence of a proper purpose, not dependent on the truth of the matter asserted, the content of the informant's tip was inadmissible hearsay.[164]

B. Purpose: Effect on the Listener

Among the more common purposes argued to remove a statement from the ambit of the hearsay rule is that the statement is being offered not to prove the truth of the matter asserted, but rather to show the statement's effect on the listener.

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157. *See* IND. R. EVID. 801(c).

158. 689 N.E.2d 1233 (Ind. 1997).

159. Mason v. State, 532 N.E.2d 1169 (Ind. 1989), *cert. denied*, 490 U.S. 1049 (1990).

160. Mason v. State, 634 N.E.2d 100 (Ind. Ct. App. 1994), *trans. denied.*

161. Mason v. Hanks, 97 F.3d 887 (7th Cir. 1996).

162. *See Mason*, 689 N.E.2d at 1236. The informant himself did not testify, and his identity remained confidential.

163. *Id.*

164. *See id.* at 1236-37 (citing Glover v. State, 251 N.E.2d 814, 818 (1969)). Because Mason's trial took place in 1986, nearly eight years before the Indiana Rules of Evidence became effective, the supreme court decided Mason's appeal under common law. The court noted, however, that the result it reached would have been the same under the Rules. *Id.* at 1237.

The Indiana Supreme Court underscored this principle in two cases during the survey period. In *Sylvester v. State*,[165] a murder prosecution, the defendant asserted that his offense was manslaughter, not murder, because it had been committed in sudden heat, based on the defendant's fear that his wife was having an affair.[166] In support of his position, the defendant attempted to introduce evidence of a discussion between the defendant and his wife, in which his wife denied having an affair. The trial court excluded the wife's statement as hearsay, but the Indiana Supreme Court concluded that this was error: The statement was not offered to prove the truth of the matter asserted, but rather to show its effect on the defendant in giving rise to sudden heat.[167]

Hirsch v. State[168] presented a slightly more complicated scenario. In *Hirsch*, the defendant and the victim were involved in a jailhouse brawl, in which the defendant inflicted injuries on the victim that ultimately proved fatal.[169] At trial, the defendant claimed self-defense. In support of his claim, he sought to testify that, during the fight, he urged the victim to cease fighting but the victim stated that he would not. The defendant also presented the testimony of several bystanders who would have corroborated his testimony. In each instance, the trial court sustained the prosecution's objection that the victim's statement was hearsay.[170] The supreme court concluded that this was error. The court noted that, pursuant to Indiana's self-defense statute, the victim's stated refusal to stop fighting was relevant to the defendant's claim of self-defense regardless of whether the statement was true.[171]

C. *Prior Consistent Statements*

Rule 801(d)(1)(B) provides that a witness's prior statement is non-hearsay if it is consistent with the witness's trial testimony and is "offered to rebut a charge of recent fabrication or improper influence or motive, and made before the motive to fabricate arose."[172] In *Parmley v. State*,[173] the Indiana Court of Appeals concluded that, where multiple charges of recent fabrication or improper influence or motive are made, a prior consistent statement is admissible as non-hearsay, provided that it predated any one of the charged improper influences or motives.[174] *Parmley* was a prosecution for child molesting. On cross-examination of the child victim (the defendant's daughter), the defendant's questioning raised several possible motives for fabrication, including: a desire

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165. 698 N.E.2d 1126 (Ind. 1998).
166. *See id.* at 1127.
167. *Id.* The court concluded that the error was harmless. *Id.* at 1130.
168. 697 N.E.2d 37 (Ind. 1998).
169. *See id.* at 38.
170. *See id.* at 38-39.
171. *Id.* at 40.
172. IND. R. EVID. 801(d)(1)(B).
173. 699 N.E.2d 288 (Ind. Ct. App. 1998).
174. *Id.* at 293.

for attention, unhappiness with the defendant for remarrying and bringing his new wife into the home, and the influence of the victim's mother.[175] The prosecutor then presented three witnesses to testify regarding the victim's prior consistent statements. The defendant argued that these statements were inadmissible because the statements did not predate the alleged motives to fabricate. The court concluded, however, that all three prior statements predated the victim's questioning by the police,[176] an occasion on which, the defendant suggested, the victim fabricated her story as a means of gaining attention.

D. Statements of Co-conspirators

Pursuant to Rule 801(d)(2)(E), a statement of a co-conspirator is not considered hearsay if it is made during the existence of and in furtherance of the conspiracy.[177] An obvious prerequisite for the application of Rule 801(d)(2)(E) is the existence of a conspiracy. The issue then arises, what proof is necessary to demonstrate the existence of the conspiracy before the co-conspirator's statement will be admitted? Prior to the adoption of the Rules, the Indiana Supreme Court rejected the boot-strapping argument that the co-conspirator statement, admission of which was sought, could itself provide sufficient evidence of the existence of the conspiracy; instead, the court required that there be independent evidence, either direct or circumstantial, of the existence of the conspiracy.[178] In *Lott v. State*,[179] the Indiana Supreme Court made clear that the requirement of independent evidence remained in effect under the Rules.[180] The testimony of a co-conspirator, describing the conspiracy, easily meets this requirement.[181]

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175. *See id.*

176. *Id.*

177. IND. R. EVID. 801(d)(2)(E).

178. Lott v. State, 690 N.E.2d 204, 209 (Ind. 1997).

179. *Id.* at 204.

180. *Id.* at 209.

181. *See id.*; *see also* Wright v. State, 690 N.E.2d 1098, 1106 (Ind. 1997). In neither *Lott* nor *Wright* did the court address the question of whether the co-conspirator statement itself could serve as some evidence, though not sufficient evidence, of the existence of the conspiracy. Federal Rule 801(d)(2) was amended, effective December 1, 1997, to provide expressly that the statement at issue may be considered in determining the existence of a conspiracy, though it is not itself sufficient to establish the point. *See* FED. R. EVID. 801(d)(2). This amendment adopted the approach taken by the federal courts of appeals that had addressed the issue. *See, e.g.*, United States v. Clark, 18 F.3d 1337, 1342 (6th Cir. 1994); United States v. Sepulveda, 15 F.3d 1161, 1181-82 (1st Cir. 1993); United States v. Gambino, 926 F.2d 1355, 1361-62 & n.5 (3d Cir. 1991); United States v. Torres, 908 F.2d 1417, 1425 (9th Cir. 1990); United States v. Whalen, 844 F.2d 529, 532-33 (8th Cir. 1988); United States v. Zambrana, 841 F.2d 1320, 1344-45 (7th Cir. 1988). In *Wright*, the Indiana Supreme Court noted that the Federal Rule was a "mirror image" of Indiana's Rule 801(d)(2)(E) and concluded that, in the absence of countervailing Indiana policies, consideration of federal cases in the interpretation of Indiana's Rule was appropriate. *Wright*, 690

E. Excited Utterances

Rule 803(2) creates an exception to the hearsay rule for statements made while under the influence of a startling event that relate to the startling event. The theory underlying the exception is that the influence of the startling event eliminates the possibility of reflection that raises the danger of insincerity and loss of memory. Unlike the exception for present sense impressions, which requires that the statement be made while perceiving the event described or immediately thereafter,[182] the exception for excited utterances does not have a strict temporal component—the exception continues to apply for as long as the excitement generated by the startling event persists. Thus, in *Carter v. State*,[183] a prosecution for robbery and attempted murder, the Indiana Supreme Court allowed the introduction of a statement made by the victim in the emergency room, shortly after the attack, because at the time of the statement the victim was still under "the stress of excitement from the startling event."[184]

Carter is also significant in its limitation of the supreme court's pre-Rules decision in *Modesitt v. State.*[185] In *Modesitt*, the supreme court held that, where the declarant testifies and cannot recall making a prior statement, the prior statement is inadmissible.[186] In *Carter*, the shooting victim did testify at trial, but, having been shot in the head three times during the incident in question, did not recall his emergency room statement. The *Carter* court held, however, that *Modesitt* does not bar admission of statements that fall within the hearsay exception for excited utterances.[187]

F. State of Physical or Mental Condition

Rule 803(3) excludes from the hearsay bar a declarant's description of a then-existing physical, mental, or emotional condition.[188] The exception only applies to then-existing conditions; it does not permit the introduction of retrospective descriptions of a previously existing condition and expressly excludes from the exception statements of memory or belief offered to prove the

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N.E.2d at 1105 n.7. The Indiana Rule, however, has not yet been amended to incorporate the new provisions of the Federal Rule.

182. IND. R. EVID. 803(1). In *Jackson v. State*, 697 N.E.2d 53 (Ind. 1998), the Indiana Supreme Court held that a statement describing a crime, made several hours after the crime, cannot qualify under the exception for present sense impressions, because the statement was not made during or immediately after the crime. *Id.* at 54.

183. 686 N.E.2d 834 (Ind. 1997).

184. *Id.* at 837.

185. 578 N.E.2d 649 (Ind. 1991).

186. *Id.* at 652.

187. *Carter*, 686 N.E.2d at 837.

188. IND. R. EVID. 803(3).

fact remembered or believed.[189] Thus, in *Jackson v. State*,[190] the Indiana Supreme Court held that the exception did not encompass the defendant's statement, made three hours after the defendant shot the victim, that the defendant had not meant to kill the victim.[191] This statement, the court concluded, did not describe the defendant's intent at the time of the statement, but rather represented a statement of a fact remembered or believed, offered to prove that fact.[192]

Of course, even if a statement fits within the Rule 803(3) exception, it may only be admitted if the declarant's then-existing physical, mental, or emotional condition is an issue in the case. In *Wrinkles v. State*,[193] the Indiana Supreme Court concluded that, in a typical murder prosecution, the murder victim's state of mind is not at issue and therefore a victim's statement describing her then-existing state of mind should not be admitted.[194] This decision would be unremarkable but for the fact that in *Bacher v. State*,[195] a majority of the supreme court concluded, over a strong dissent by Justice Boehm (in which Justice Dickson joined) that evidence of a murder victim's state of mind could be introduced.[196] While it is true that the *Bacher* court did not allow the victim's statement to be used as evidence of the defendant's subsequent conduct, the court implicitly concluded that the victim's state of mind was a relevant issue in the trial, even though no argument as to that relevance appears to have been made.[197] The *Wrinkles* decision did not cite *Bacher*. Given the lack of citation, it is not clear whether the court now intends to cabin *Bacher* as a narrow decision that does not open the door generally to admission of victims' statements of state of mind in murder prosecutions, or whether *Wrinkles* is itself aberrational.

G. Business Records

Rule 803(6) permits the introduction of business records that are made at or near the time of the events recorded, derived from information provided by a person with knowledge, and regularly kept in the course of business.[198] In *Schloot v. Guinevere Real Estate Corp.*,[199] the Indiana Court of Appeals confronted the question of whether Rule 803(6) permitted the introduction of

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189. *Id.*
190. 697 N.E.2d 53 (Ind. 1998).
191. *Id.* at 54-55.
192. *Id.*
193. 690 N.E.2d 1156, 1159 (Ind. 1997).
194. *Id.* at 1159.
195. 686 N.E.2d 791 (Ind. 1997). *Bacher*, which was decided near the beginning of this survey period, received extensive treatment in last year's survey. *See* O'Brien, *supra* note 78, at 614-16.
196. *Bacher* was a highly problematic decision for reasons that are thoroughly explained in last year's survey. *See* O'Brien, *supra* note 78, at 615-16.
197. *Bacher*, 686 N.E.2d at 797.
198. IND. R. EVID. 803(6).
199. 697 N.E.2d 1273 (Ind. Ct. App. 1998).

medical records containing medical opinions and diagnoses. *Schloot* involved a slip-and-fall accident. The plaintiff attempted to introduce her medical records, which reflected the extent of her injuries following her fall. The court of appeals concluded that the admission of the records was error on two grounds. First, the court concluded that compliance with Rule 803(6) did not itself guarantee admissibility. Compliance with other rules was required as well, and Rule 702 required testimony for the admission of expert opinion.[200] Second, the court suggested that, even if the requirements of Rule 702 were left aside, the medical records should not be admitted as business records under Rule 803(6). In so concluding, the court relied on *Fendley v. Ford*,[201] a 1984 case in which the court of appeals had refused to admit medical records on the grounds that such records, standing alone, did not have sufficient indications of trustworthiness; the accuracy of the records could not be tested in the absence of cross-examination.[202] The court recognized that *Fendley* predated the adoption of the Indiana Rules of Evidence by a decade, but concluded that its rationale remained persuasive under the Rules.[203]

Schloot raises an interesting interpretive issue. On one level, the court's conclusion seems sound. A medical diagnosis from a particular set of observed facts may well involve the formation of opinions as to which reasonable physicians might differ. Given that reality, the presentation of a medical diagnosis through a business record, without the possibility of cross-examination, seems problematic. Indeed, courts in a number of states have concluded that records containing medical opinions, rather than factual observations, do not meet the requirements of the business record exception and are therefore inadmissible hearsay.[204] On the other hand, Rule 803(6) appears to contemplate, by its terms, that medical opinions, if regularly generated and kept, may qualify as business records: The Rule's description of what items may constitute business records includes both "opinions" and "diagnoses."[205] The *Fendley* court's conclusion that documents containing medical diagnoses cannot qualify as business records, therefore, would appear now to be foreclosed by the text of the rule itself.[206] A better ground for the *Schloot* court's decision would seem to be its reference to Rule 702, which provides for the presentation of expert

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200. *See id.* at 1277.

201. 458 N.E.2d 1167 (Ind. Ct. App. 1984).

202. *Schloot*, 697 N.E.2d at 1277 (citing *Fendley*, 458 N.E.2d at 1171 n.3).

203. *Id.*

204. *See, e.g.*, Durant v. United States, 551 A.2d 1318, 1323-24 (D.C. 1988); State v. Garlick, 545 A.2d 27, 32 (1988) (quoting Gregory v. State, 391 A.2d 437, 454 (1978)); State v. Key, 284 S.E.2d 781, 783 (1981).

205. IND. R. EVID. 803(6). At least one federal court has concluded, on the basis of the identical passage in the parallel federal rule, that Rule 803(6) does permit the introduction, as business records, of records incorporating medical opinions. *See* Manocchio v. Moran, 919 F.2d 770, 779 (1st Cir.), *cert. denied*, 500 U.S. 910 (1990).

206. *Cf. Manocchio*, 919 F.2d at 779 (finding that by its terms, Federal Rule of Evidence 803(6) permits the introduction of medical records containing diagnoses).

opinion through live testimony. The question remains, however, why Rule 803(6) would include references to "opinions" and, especially, "diagnoses" if the drafters of the Rules believed that opinions and diagnoses required the testing of cross-examination per se to be admissible. In light of these uncertainties, further consideration of the issues addressed in *Schloot* seems necessary.

HEALTH CARE LAW: A SURVEY OF SIGNIFICANT 1998 DEVELOPMENTS

JOHN C. RENDER*
JAMES B. HOGAN**

INTRODUCTION

This Article reviews significant developments in the divergent field of health care law. The primary focus of this Article is on those areas which most likely impact client concerns, and therefore are of the most utility to practitioners in this field. This Article is not intended to be a comprehensive analysis of the most recent changes, but instead encapsulates several of the most important health care issues, including the new Stark II regulations, medical malpractice, Medicare and Medicaid issues, antitrust, labor and employment, fraud and abuse, and legislative health initiatives.

I. FEDERAL DEVELOPMENTS

A. Federal Stark II Legislation

On January 9, 1998, the Health Care Financing Administration ("HCFA") issued proposed regulations[1] for sections 1877 and 1903(s) of the Social Security Act ("SSA"), better known as the Stark II Act.[2] Stark II restricts physician referrals for certain "designated health services" to entities with which they or immediate family members have a financial interest.[3] The scope of Stark II is extremely comprehensive, applying to practically any financial arrangement involving a physician or immediate family member.[4] However, HCFA's interpretations of certain statutory terms, as well as the additional requirements imposed in certain definitions and exceptions, raise many issues for providers. The proposed regulations are extremely detailed and provide additional insight into the law's referral prohibitions, specifically defining each designated health service.[5]

Stark II provides that if a physician or member of a physician's immediate family has a financial relationship with a health care entity, "the physician may

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* Partner, Hall, Render, Killian, Heath & Lyman, P.S.C. B.S., 1966, Butler University; J.D., 1971, Indiana University School of Law—Indianapolis.

** Associate, Hall, Render, Killian, Heath & Lyman, P.S.C. B.A., Hanover College; J.D., 1994, Indiana University School of Law—Indianapolis. The authors would like to thank the following persons for their contributions: Gregg Wallander, Esq., Clifton E. Johnson, Esq., Letha S. Kramer, Esq., Angela Smith, Esq., John P. Ryan, Esq., and Timothy A. McGeath.

1. Health Care Financing Administration, 63 Fed. Reg. 1659 (1998) (to be codified at 42 C.F.R. pt. 411, 424, 435 & 455).
2. The Public Health & Welfare Act § 18, 42 U.S.C. § 1395nn (1994).
3. *Id.* § 1395nn(a).
4. *Id.*
5. 63 Fed. Reg. at 1663-64.

not make a referral to the entity for the furnishing of designated health services" for which payment may be made under the Medicare/Medicaid programs.[6] Further, the entity may not present a claim to Medicare/Medicaid or bill any third party payor for services furnished pursuant to a prohibited referral.[7]

HCFA, in its proposed regulations, utilizes the Medicare definition of physician, which includes an M.D. or D.O., dentist or oral surgeon, podiatrist, optometrist, and chiropractor.[8] "Immediate family member" means husband or wife; natural or adoptive parent, child or sibling; step relatives (parent, child, brother, sister); in-laws (father, mother, son, daughter, brother, sister); grandparent or grandchild; and spouse of a grandparent or grandchild.[9]

The term "financial relationship," whether direct or indirect, refers to ownership or investment interest in an entity or compensation arrangement with an entity.[10] A "compensation arrangement" means any arrangement involving any remuneration between a physician (or immediate family member) and an entity.[11] The term "remuneration" includes any payment, discount, forgiveness of debt, or other benefit made directly or indirectly, in cash or in kind.[12]

The term "referral" is broadly worded to include a request for any designated health service payable under Medicare or Medicaid.[13] A request by a pathologist for clinical diagnostic laboratory services, by a radiologist for radiology services, or by a radiation oncologist for radiation therapy services, is not deemed to be a referral if such request results from a consultation initiated by another physician and such tests or services are furnished by or under the supervision of such pathologist, radiologist, or radiation oncologist.[14]

In the proposed regulations, HCFA defines each of the statutory designated health services.[15] Except for inpatient hospital services and home health services, these definitions are based upon how Medicare covers a service under Part B.[16] For purposes of Medicaid, the Medicare definitions will still apply unless a state definition differs, in which case the state definition will apply.[17]

HCFA believes that a designated health service remains one, even if it is billed as something else or is subsumed within another service category by being bundled with other services for billing purposes.[18] As an example, services performed by a skilled nursing facility ("SNF") are considered SNF services,

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6. 42 U.S.C. § 1395nn(a).
7. *See id.*
8. 63 Fed. Reg. at 1704.
9. *Id.* at 1721-22 .
10. *Id.* at 1721.
11. *Id.* at 1720.
12. *Id.* at 1723.
13. *Id.* at 1722-23.
14. *Id.*
15. *See* The Public Health & Welfare Act § 18, 42 U.S.C. § 1395nn (1994).
16. *See* 63 Fed. Reg. at 1673-74.
17. *See id.*
18. *See id.* at 1673.

which are not themselves designated health services.[19] Nonetheless, SNF services can encompass a variety of designated health services, such as physical therapy or laboratory services.[20] In sum, HCFA interprets a designated health service as one provided regardless of the setting in which it is provided or payment category under which it is billed.[21] This interpretation is thus very broad and includes both the professional and technical components of a service.[22]

The proposed regulations contain clarification of the exceptions found in the Stark legislation as well as add new exceptions.[23] These exceptions apply to (i) both an ownership/investment interest and a compensation arrangement, (ii) only an ownership/investment interest, or (iii) only a compensation arrangement.[24] Providers must be careful to meet the correct exceptions under the law.

Exceptions for both ownership/investment interests and compensation arrangements include "physician" services, in-office ancillary services, services furnished through certain government prepaid plans, and services furnished under ambulatory surgery center, end stage renal disease, or hospice rates.[25] Exceptions solely for ownership/investment interests include ownership of certain publicly traded securities, certain rural providers, and hospitals.[26]

Exceptions for compensation arrangements include space and equipment rentals, bona fide employment relationships, personal service arrangements, physician recruitment arrangements, isolated transactions, certain unrelated and group practice arrangements with hospitals, certain payments for items or services furnished, discounts, *de minimis* compensation, and fair market value compensation arrangements.[27] Each of these exceptions has numerous requirements which must be met in full to escape Stark's prohibitions.

The proposed regulations contain significant developments of which providers must be aware. HCFA's interpretations of the group practice definition are among the most significant developments in the proposed regulations. Highlights include a requirement that the group be a single legal entity; a group may have more than one billing number as long as such billing numbers are assigned to the group.[28] Further, physician owners and employees are only deemed "members of the group" if they meet the applicable seventy-five percent threshold standards for providing services through the group, as well as the group members providing at least seventy-five percent of the total patient case for the group.[29] In other words, independent contractors may not be utilized by a group

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19. *See id.*
20. *See id.*
21. *See id.*
22. *See id.*
23. *See id.* at 1723-26.
24. *See id.*
25. *See id.* at 1723-24.
26. *See id.* at 1724.
27. *See id.* at 1724-26.
28. *See id.* at 1721.
29. *See id.* at 1722.

to meet the in-office ancillary services exception.

Group practices must also meet internal accounting and compensation requirements. Most notably, distribution of profits may not be based directly on referrals for designated health services—*even* self-referrals.[30] In addition, all compensation and overhead methodologies must be set in advance of the period in which the applicable services are performed and reflect a unified business as opposed to satellite offices acting as separate enterprises.[31]

The In-Office Ancillary Services for both ownership/investment interests and compensation arrangements includes three requirements that apply to the performance, location and billing of such services.[32] Regarding the performance component, çertain in-office ancillary services may be performed by an individual who is directly supervised by the referring physician or another physician in the same group practice as the referring physician.[33] The regulations define "direct supervision" as supervision by a physician who is actually present in the office suite and immediately available to provide assistance and direction throughout the time services are performed.[34]

Regarding the location component, the services must be provided in the same office in which a physician provides actual physician services, a building used by a group for the provision of some or all of the group's clinical laboratory services, or a building used by a group for the centralized provision of the group's designated health services (other than clinical laboratory services).[35] Finally, although the in-office ancillary services exception does not apply to durable medical equipment ("DME"), a physician may provide crutches as long as no direct or indirect profit is realized.[36]

HCFA defines "fair market value" to mean the value in arm's length transactions, consistent with general market value.[37] "General market value" is an asset price or service compensation which is the result of bona fide bargaining between well-informed buyers and sellers or parties to an agreement.[38] According to HCFA, the fair market price is usually the price at which bona fide sales have been consummated for assets of like type, quality, and quantity in a particular market at the time of acquisition, or the compensation that has been included in bona fide service agreements with comparable terms at the time of the agreement.[39] With respect to rentals and leases, fair market value includes that for general commercial purposes (not taking into account its intended use) which may not be adjusted to reflect the additional value with respect to

30. *See id.* at 1721.
31. *See id.*
32. *See id.* at 1723.
33. *See id.*
34. *Id.* at 1720.
35. *See id.* at 1723.
36. *See id.*
37. *Id.* at 1721.
38. *Id.*
39. *Id.*

proximity or convenience of referrals.[40]

The proposed regulations reiterate that compensation may not fluctuate in a manner that reflects referrals,[41] including situations where a physician's payments are stable but predicated, *either expressly or otherwise*, on the physician's referrals to a particular provider.[42] For example, if a physician is required to refer to an entity as a condition of employment, such compensation is deemed to impermissibly take into account the volume or value of referrals, even if the compensation is otherwise stable.[43] This interpretation is potentially problematic and seems to ignore many standard health care contracts, such as exclusive relationships, employee/contractor covenants not to compete, and other managed care initiatives.

HCFA proposes to create a compensation arrangement exception for *de minimis* compensation.[44] This exception places limits on compensation from an entity in the form of items or services (not including cash or cash equivalents) that does not exceed $50 per gift and an aggregate of $300 per year.[45] Such compensation must be provided to all similarly situated individuals, regardless of whether these individuals refer patients, and cannot be based in any way upon referrals.[46]

A proposed exception covering other written contracts at fair market value also exists. However, among other requirements, this exception requires that the arrangement meet a safe harbor regulation under the Anti-Kickback Statute[47] or otherwise be in compliance with the Anti-Kickback law.[48] Because it is difficult to meet a safe harbor regulation[49] under the Anti-Kickback Statute, it remains unclear whether this exception will be truly beneficial.

The proposed regulations require all entities furnishing items or services for which payment may be made under Medicare to submit information to HCFA concerning their financial relationships as defined under Stark II.[50] This information must be submitted on a HCFA-prescribed form within the time period specified by the servicing carrier or intermediary.[51] Thereafter, an entity must report annually to HCFA all changes that occurred in the previous year.[52] The sanctions for failure to meet this reporting requirement include civil penalties of up to $10,000 for each day after the provider's application deadline

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40. *See id.*
41. *Id.* at 1699-1700.
42. *Id.* at 1700.
43. *See id.*
44. *Id.* at 1725.
45. *Id.*
46. *See id.*
47. *Id.* at 1725-26; *see* 42 C.F.R. § 1001.952 (1998).
48. 63 Fed. Reg. at 1725-26; *see* 42 C.F.R. § 1001.952.
49. *See* 42 C.F.R. § 1001.952.
50. 63 Fed. Reg. at 1726-27.
51. *See id.*
52. *See id.*

that a report is not properly made.[53]

In sum, every financial arrangement involving physicians and their immediate family members should be separately scrutinized under Stark II. Sanctions for violating the statute include civil penalties of up to $15,000 for submitting an illegal claim or not refunding such a claim on a timely basis (within sixty days) and up to $100,000 for each circumvention arrangement or scheme.[54]

On the same day that the Stark II proposed regulations were issued, HCFA also issued final regulations outlining a process for advisory opinions.[55] This process allows any individual or entity to request a written advisory opinion from HCFA concerning whether a physician's referrals for designated health services (other than clinical laboratory services) to an entity is or would be prohibited under Stark II and whether an exception applies.[56] However, HCFA will not advise whether an arrangement is at fair market value or whether an individual is a bona fide employee under the Internal Revenue Code.[57]

B. Federal Anti-Kickback Statute Advisory Opinions

On July 16, 1998, the Department of Health and Human Services Office of Inspector General ("OIG") issued a final rule for the issuance of Anti-Kickback Statute advisory opinions.[58] Several advisory opinions have already been issued.

1. Advisory Opinion 97-4.[59]—This opinion addresses whether the decision by an ambulatory surgery center ("ASC") to decline to pursue collection of copayments from patients with employer-sponsored Medicare complementary coverage constitutes grounds for imposition of sanctions under the Health Insurance Portability and Accountability Act ("HIPAA")[60] or the Anti-Kickback Statute.[61] Based on the OIG's review, any waiver of the copayment obligation constitutes remuneration to the beneficiary. Further, the ASC's proposal to refrain from pursuing collection of the Medicare copayment from beneficiaries is intended, at least in part, to encourage covered beneficiaries to obtain services at the ASC. The proposed arrangement would therefore potentially be subject to sanction under HIPAA.[62]

The OIG noted that when providers forgive financial obligations for reasons

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53. *Id.*

54. The Public Health & Welfare Act § 18, 42 U.S.C. § 1395nn(g) (1994).

55. 63 Fed. Reg. at 1646.

56. *See id.* at 1655.

57. *See id.*

58. Advisory Ops. by the Off. of Inspector Gen., 42 C.F.R. §§ 1008.1-.59 (1998). This final rule follows an interim final rule published February 19, 1997. *See id.*

59. 97 Op. Off. of Inspector Gen. No. 97-4 (Sept. 25, 1997) [hereinafter No. 97-4].

60. Health Insurance Portability & Accountability Act of 1996, 42 U.S.C. §§ 1320a-7a(a), -7(a)(5) (1994 & Supp. II 1996).

61. 42 U.S.C. § 1320a-7b(b) (1994 & Supp. II 1996).

62. *See* No. 97-4, *supra* note 59.

other than genuine financial hardship of the particular patient, they may be unlawfully inducing the patient to purchase items or services in violation of the Anti-Kickback Statute's proscription against offering or paying something of value as an inducement to generate business payable by a federal health care program. Thus, except in those special cases of financial hardship, providers must make a good faith effort to collect Medicare copayments.[63]

2. *Advisory Opinion 97-6.*[64]—The OIG considered whether a proposed arrangement for restocking ambulance supplies and medications at no charge to ambulance services operated by a governmental entity constitutes illegal remuneration as defined in the Anti-Kickback Statute.[65] The OIG concluded that the hospitals' proposed provision of free supplies and medications to a municipal ambulance services fits squarely within the meaning of remuneration for purposes of the Anti-Kickback Statute.[66] An inference may be drawn that at least one purpose of this remuneration may be to induce the ambulance services to bring patients to the hospitals. To the extent those patients include beneficiaries of federal health care programs who require covered hospital services, the Anti-Kickback Statute may be implicated.

This proposed arrangement poses a risk of improper steering of patients and unfair competition. Patients in need of ambulance services are often in a vulnerable state, and their choice of emergency room may be influenced by ambulance service personnel. In these circumstances, where the payments relate directly to the delivery of patients, remuneration paid by a hospital to an ambulance service, including the provision of free goods, would be highly suspect. Although there may be no intent to induce referrals by such a practice (and such a practice may be fairly common), the OIG has decided that the parties may be at high risk for violating the Anti-Kickback Statute for such acts.[67] Hospitals that have relationships with ambulance services should review such relationships accordingly.

This Advisory Opinion has been the subject of much debate in the health care industry, and the concept of restocking and offering items to ambulance providers has been the subject of other Advisory Opinions. In Advisory Opinion 98-3,[68] the OIG approved the donation of an ambulance to a municipal fire department. In Advisory Opinion 98-7,[69] the OIG approved of a coordinated effort by a city council to restock ambulances with supplies and medications. This council had representation from the provider community and was responsible for oversight of the program. Finally, in Advisory Opinion 98-13,[70] the OIG approved of an ambulance restocking program coordinated through a

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63. *See id.*

64. 97 Op. Off. of Inspector Gen. No. 6 (Oct. 8, 1997) [hereinafter No. 97-6].

65. 42 U.S.C. § 1320a-7b(b).

66. No. 97-6, *supra* note 64.

67. *Id.*

68. 98 Op. Off. of Inspector Gen. No. 3 (April 14, 1998).

69. 98 Op. Off. of Inspector Gen. No. 7 (June 16, 1998).

70. 98 Op. Off. of Inspector Gen. No. 13 (Sept. 23, 1998).

local emergency medical services council. In approving these initiatives, the OIG takes comfort in the increased quality of care to the respective communities and the minimal risk of abuse.

C. *Internal Revenue Service Intermediate Sanction Regulations*

In July 1998, the Internal Revenue Service ("IRS") proposed intermediate sanction regulations that impose penalties on "disqualified persons" engaging in "excess benefit transactions" with organizations exempt from federal income taxation under Internal Revenue Code § 501(c)(3) or (c)(4) as well as the "organization managers" who consent to such transactions.[71] Prior to the September 1995 enforcement of Internal Revenue Code § 4958, the only legal remedy available to the IRS when an exempt entity engaged in a prohibited transaction was to revoke the entity's tax-exempt status.[72] The IRS was historically hesitant to impose such a drastic sanction.

The intermediate sanction regulations (the "Rules") that proposed to alter Internal Revenue Code § 4958 broaden the tax penalty remedies and the definition of a "disqualified person."[73] The Rules allow for the imposition of a two-tiered penalty tax upon any "disqualified person" who engages in an excess benefit transaction with a § 501(c)(3) or (c)(4) tax-exempt organization.[74]

An "excess benefit transaction" is defined as any deal in which a § 501(c)(3) or (c)(4) tax-exempt organization provides, either directly or indirectly, an economic benefit to a disqualified person where the value of such benefit exceeds the value received by the organization in return.[75]

A "disqualified person" is defined by statute as any person involved in a transaction in a position to exercise substantial influence over the exempt entity's affairs at any time during the prior five year period ending on the date of the transaction.[76] The Rules extend this definition to apply to the family members of a disqualified person, as well as any entity in which a disqualified person either directly or indirectly owns more than a thirty-five percent interest.[77]

The first-tier tax imposed by the Rules is an excise tax equal to twenty-five percent of any excess benefit a disqualified person receives from an improper economic benefit.[78] If the excess benefit transaction is not timely corrected, the disqualified person is subject to a second-tier tax of two hundred percent of the excess benefit received.[79] In addition to the excise taxes imposed on the

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71. Department of Treasury, 63 Fed. Reg. 41,486 (1998) (to be codified at 26 U.S.C. § 4958)).
72. 26 U.S.C. § 4958 (Supp. II 1996).
73. 63 Fed. Reg. at 41,486.
74. *Id.* at 41,489.
75. 26 U.S.C. § 4958(c)(1)(A); 63 Fed. Reg. at 41,491.
76. 26 U.S.C. § 4958(f)(1).
77. 63 Fed. Reg. at 41,490.
78. *Id.* at 41,489.
79. *See id.*

disqualified person taking part in the excess benefit transaction, any exempt organization manager who approved the excess benefit transaction knowing it to be improper may be subject to a separate tax of ten percent of the excess benefit, not to exceed $10,000 for each separate transaction.[80]

Of significant interest are the comments from the House Report, which state that physicians are not intended to be treated as "per se" disqualified persons, looking instead to the facts and circumstances of each situation to make this determination.[81] This departs from the prior guidance in this area, where the IRS took the position that physicians were insiders with regard to exempt entities where they render professional medical services, and therefore, all transactions between such organizations and these physicians were traditionally subject to an inference of private inurement.[82]

Examples of "disqualified persons" include any voting member of an exempt entity's governing body, as well as the president, chief executive officer, chief operating officer, treasurer and chief financial officer of the organization.[83] However, in determining who is a disqualified person, the IRS will look to the individual's actual responsibilities and authority rather than his title.[84] If a person does not fall directly within the definition of "disqualified persons," the IRS will apply a facts and circumstances test to make this determination.[85] The Rules set out a series of non-exclusive facts and circumstances which the IRS believes tend to reflect that an individual has substantial influence over an exempt organization.[86] Additionally, the IRS has listed facts and circumstances which reflect that an individual is not a disqualified person.[87]

These Rules offer significant guidance in the area of hospital-physician transactions, particularly with regard to the reasonableness of compensation paid to physicians.[88] The Rules specify that compensation will be deemed reasonable if it is an amount which would customarily be paid for similar services "by like enterprises under like circumstances."[89] The parties can establish a rebuttable presumption of reasonableness by having a compensation package approved by an independent board or board subcommittee unrelated to the subject or control of the disqualified person provided that the board or subcommittee obtains and relies upon appropriate compensation comparability data and adequately

80. *See id.*

81. H.R. REP. NO. 506 at 43 n.12 (1998).

82. IRS Gen. Couns. Mem. 39862 (Nov. 22, 1991); IRS Gen. Couns. Mem. 39498 (April 24, 1986); IRS Announcement 92-83, *Exempt Organizations; Examination Guidelines for Hospitals* § 33.2(2) (June 1, 1992).

83. 63 Fed. Reg. at 41,490.

84. *See id.*

85. *See id.*

86. *Id.*

87. *Id.*

88. *See id.* at 41,191-92.

89. *Id.*

documents the basis for any determinations it makes.[90]

D. IRS Revenue Ruling 98-15

On March 4, 1998 the IRS provided significant guidance in the area of tax-exempt organizations.[91] In Revenue Ruling 98-15, the IRS addressed two scenarios in which a tax-exempt hospital, by contributing all of its operating assets to a joint venture, forms a limited liability company (LLC) with a for-profit corporation. In the first hypothetical situation, the LLC's governing documents provide for a five person governing board, with three of the five directors selected by the nonprofit hospital. The governing documents could only be amended with the approval of both owners, and a majority of directors was required to approve key decisions related to the LLC's operations.[92] Also, the governing documents specifically required that the LLC operate any hospital it owns in a manner that furthers charitable purposes. This structure was treated as a "safe harbor" by the IRS.[93]

In contrast, the LLC's governing documents in the second hypothetical situation provided for a six person board, with three directors selected by each member. The governing documents could only be amended with approval of both members, and a majority of the entire board was required for a more limited list of operating decisions. The governing documents did not provide that the LLC operate any healthcare facilities it owns in a manner to further their charitable purposes. This approach was deemed violative of IRS statute and would jeopardize the tax-exempt entity's exempt status.[94]

The IRS reiterated that a section 501(c)(3) organization may enter into a partnership-like venture, including an LLC, so long as the venture furthers a charitable purpose and allows the exempt organization to act exclusively in furtherance of its exempt purpose.[95] In addition to the "purpose test," Revenue Ruling 98-15 focused on the "control test"—whether the exempt hospital retains sufficient control over the activities of the venture as to prevent more than an incidental private benefit to the for-profit entity.[96]

Through Revenue Ruling 98-15, the IRS identified key factors in deciding whether activities related to a joint venture between exempt and non-exempt entities are in furtherance of the exempt organization's charitable purposes. With regard to the "purpose test," the governing documents should require the new

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90. *See* H.R. REP. NO. 506 at 41 (1998).

91. Rev. Rul. 98-15 (Mar. 4, 1998).

92. The decisions related to the following topics: the LLC's annual capital and operating budgets, distributions of the LLC's earnings, selection of key executives, acquisition or disposition of health care facilities, contracts in excess of a certain dollar amount, changes to the types of services offered by the hospital, and renewal or termination of management agreements. *See id.*

93. *Id.*

94. *See id.*

95. *Id.* (citing Plumstead Theatre Society, Inc. v. Commissioner, 74 T.C. 1324 (1980)).

96. *Id.*

entity to serve charitable purposes or provide health care services to the community as a whole. Moreover, furtherance of charitable purposes must override any duty to provide financial benefit to the owners. However, by emphasizing the factors of control in both hypotheticals, the IRS clearly indicated the importance of the nonprofit hospital owner retaining sufficient control over the joint venture to ensure that its assets and activities are used primarily for charitable purposes.[97]

According to Revenue Ruling 98-15, the key powers should be reserved to the exempt organization or to a majority vote of the nonprofit owner's representatives on the board. In addition to the board's structure and voting control, the exempt organization should ensure that the joint venture be managed by an unrelated party, or that the powers of the management entity not be so broad as to effectively shift control from the board to the management company.[98]

It remains to be seen how Revenue Ruling 98-15 will affect joint ventures beyond the "whole hospital" examples discussed in the ruling. The impact could be dramatic if the same analysis is applied to physician-hospital joint ventures. Even so, the hypothetical examples presented in Revenue Ruling 98-15 represent rather extreme fact patterns and do not provide indications as to what, if any, arrangements between the two extremes might be acceptable.[99]

E. Organ Procurement Regulations

The centerpiece of the Department of Health and Human Services' 1998 initiative to increase organ, tissue, and eye donation was a set of regulations which established new organ procurement guidelines for hospitals.[100] The federal regulations became effective on August 21, 1998.[101] Hospital compliance with these new regulations is a condition for participating in the Medicare and Medicaid programs.[102]

The regulations principally address three key topics. First, responsibility for determining an individual's medical suitability for organ donation will shift from hospitals to organ procurement organizations ("OPO").[103] The new rule requires

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97. *Id.*

98. *See id.*

99. *Id.*

100. Department of Health & Human Servs., 63 Fed. Reg. 33,856 (1998) (to be codified at 42 C.F.R. pt. 482).

101. *Id.* The final rule was published on June 22, 1998. Hospitals have one full year from the date the final rule took effect to come into compliance. Enforcement will begin on August 21, 1999. *See id.*

102. *See id.* An example of a compliance regulation is section 1320b-8 of the Public Health & Welfare Act. It requires Medicare and Medicaid participating hospitals that perform transplants to be members of the Organ Procurement and Transplantation Network and abide by its rules and requirements. 42 U.S.C. § 1320b-8(B) (1994).

103. *See* 63 Fed. Reg. at 33,856.

hospitals to have a written agreement with an OPO, under which the hospital will provide the OPO, or a third party designated by the OPO, with routine referrals of all deaths that occur in the hospitals.[104] The hospital must also have a written agreement with at least one tissue bank and at least one eye bank.[105] Finally, the regulations strengthen the consent and education process by requiring that only OPO personnel or other properly trained individuals consult with the families of potential donors.[106]

The final rule adopts "routine referral language," which requires timely hospital referral of all patient deaths, as well as information about individuals whose deaths are imminent, to the designated OPO.[107] This provision is intended to relieve the hospital of its responsibility to keep current with changing donor criteria and determine the medical suitability of potential organ donors. However, the Health Care Financing Administration ("HCFA") declined to establish federal criteria defining medically suitable donors. Instead, the OPOs have the authority under the law to conduct testing, review medical records, and gather other medical information needed to determine the medical suitability of potential donors.[108]

The final rule also shifts responsibility from the hospitals to OPOs to obtain consent from the families of potential donors.[109] HCFA found that rates of consent for organ donation are much higher when the request is made by the OPO in conjunction with the hospital staff.[110] Consequently, the final rule requires that only OPO representatives or individuals trained by the OPO may approach families to explain their donation options and make the actual request for donation.[111] The rule also allows the hospital to choose the individual who will initiate the request for donation, provided that individual has been properly educated in the consent process.[112] Hospitals are required to work cooperatively with the OPO, tissue bank and eye bank in educating staff on donation issues, as well as reviewing death records to improve identification of potential donors.[113]

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104. *See id.*

105. *See id.*

106. *Id.*

107. *Id.* at 33,858-59. The regulations do not define at what point death is "imminent," but do provide that the requirement for timely referral at death or when death is imminent means that hospitals must make referrals both before a potential donor is removed from a ventilator and while the potential donor's organs are still viable. *See id.* at 33,866.

108. *See id.* at 33,862.

109. *Id.* at 33,856.

110. *See id.* at 33,860. According to the study cited, there was a 67% consent rate when the OPO coordinator approached the family alone, a 9% rate when hospital staff approached the family alone, and a 75% consent rate when the approach was made by the OPO coordinator and hospital staff together. *See id.* (citing J. Klieger et al., *Analysis of Factors Influencing Organ Donation Consent Rates*, J. TRANSPLANT COORDINATION (1994)).

111. 63 Fed. Reg. at 33,856.

112. *Id.*

113. *See id.*

F. Antitrust

Antitrust enforcement activity maintained an aggressive pace during the 1998 fiscal year, especially in the area of mergers and acquisitions. The merger wave, which began in 1991, continued with a record 4640 Premerger Notification filings submitted to the Federal Trade Commission ("FTC") Premerger Notification Office during the fiscal year 1998.[114] Of particular interest to healthcare attorneys was the FTC's challenge of a hospital merger in Poplar Bluff, Missouri[115] and its successful effort to block two mergers of prescription drug wholesale distributors.[116] In addition, two "virtual mergers" were challenged in the fiscal year 1998.[117]

1. Federal Trade Commission v. Tenet Healthcare Corp.—In July, a federal district court in Missouri preliminarily enjoined Tenet Healthcare Corporation, which owned 201-bed Lucy Lee Hospital in Poplar Bluff, from acquiring the only other hospital in town, 230-bed Doctors Regional Medical Center, for $40.5 million.[118] The merging hospitals were each other's primary competitor in their relatively isolated service areas.

As with many antitrust merger cases, a determinative issue before the *Tenet* court was the definition of a relevant geographic market.[119] It was undisputed that Lucy Lee and Doctors Regional drew ninety percent of their patients from a service area radiating approximately fifty miles from Poplar Bluff. This service area, proffered by the FTC, included the merging hospitals and five small, rural hospitals, one of which was also owned by Tenet. The defendants, on the other hand, asserted a geographic market radiating sixty-five air miles (up to ninety-five driving miles) from Poplar Bluff, which encompassed an additional fifteen hospitals. However, the court found that statistical evidence could not, by itself, clearly define a relevant geographic market.[120]

The *Tenet* court considered anecdotal evidence from third party payors and employers within the Poplar Bluff area. The court noted that the merging hospitals had a history of negotiating deeper discounts with payors that excluded

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114. *See* Joseph G. Krauss, *New Developments in the Premerger Notification Program* (presented before the District of Columbia Bar Association, Antitrust, Trade Regulation and Consumer Affairs Section, Antitrust Committee on October 7, 1998, *available at* <http://www.ftc.gov/ os/1998/9810/dcbar.htm> (last modified Oct. 29, 1998)).

115. Federal Trade Comm'n v. Tenet Healthcare Corp., 17 F. Supp. 2d 937 (E.D. Mo. 1998).

116. Federal Trade Comm'n v. Cardinal Health, Inc., 12 F.Supp. 2d 34 (D.D.C. 1998).

117. New York v. St. Francis Hosps., No. 98-0939 (S.D.N.Y. Feb. 10, 1998); Christine Ngeo, *Partners Try Two-Step: FTC Investigates Second Phase of N.Y. Hospital Deal*, MODERN HEALTHCARE, Feb. 16, 1998, at 24.

118. *Tenet Healthcare Corp.*, 17 F. Supp. 2d at 939.

119. *Id.* at 941-42. The parties agreed that the relevant product market encompassed general acute care inpatient hospital services, including primary and secondary services, but excluding tertiary and quaternary care hospital services. *See id.* at 942.

120. *Id.*

the other local hospital from their managed care networks, and that payors believed they would be unable to negotiate the same discounts after the merger in the absence of such competition.[121] The court concluded that the more restrictive market asserted by the FTC was appropriate and that the defendants' proposed market was "inconsistent with the economic realities of Southeast Missouri."[122]

Tenet exemplifies the need to carefully balance subjective, anecdotal payor evidence against quantitative patient migration statistics.[123] Patient flow statistics do not clearly show where patients could turn in the face of competitive pricing.

2. *Federal Trade Commission v. Cardinal Health, Inc.*—On July 31, 1998, the U.S. District Court for the District of Columbia issued a preliminary injunction blocking the proposed mergers of the four largest drug wholesalers in the country.[124] In this case, the FTC sought to enjoin the merger of Cardinal Health, Inc. and Bergen-Brunswig Corporation (the second and third largest pharmaceutical wholesalers), and the merger of McKesson Corporation and AmeriSource Health Corporation (the largest and fourth largest pharmaceutical wholesalers). The proposed mergers would have reduced the number of national pharmaceutical wholesalers from four to two, creating a duopoly that "clearly would dominate the competition with close to eighty percent of the pharmaceutical wholesale market."[125]

One of the pivotal issues in the court's analysis was the relevant product market.[126] The parties conceded that pharmaceutical products are sold through four distribution channels, including national wholesale distributors, manufacturers selling directly on an as-needed basis, manufacturers buying directly coupled with self-warehousing, and mail order distributors. The FTC contended that the national wholesaler distribution channel was a distinct product market, accounting for $54 billion of the $94 billion in pharmaceutical sales in the United States during 1997.[127] The defendant drug wholesalers asserted that the relevant market encompassed all four distribution channels.[128]

The court sought to determine whether it would be reasonable for customers to switch to alternative sources of supply if the defendants were to raise prices after the proposed mergers. The court concluded that there was sufficient

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121. *Id.* at 943.

122. *Id.* at 945.

123. *Compare* Federal Trade Comm'n v. Freeman Hosp., 69 F.3d 260 (8th Cir. 1995) (supporting dynamic market analysis), *with* United States v. Long Island Jewish Med. Ctr., 983 F.Supp. 121 (E.D.N.Y. 1997) (relying heavily on patient migration statistics).

124. Federal Trade Comm'n v. Cardinal Health, Inc., 12 F. Supp. 2d 34, 34 (D.D.C. 1998).

125. *Id.* at 53.

126. *See id.* at 49-50. The parties agreed, and the court found, that the wholesale pharmaceutical industry is largely driven by competition on a national level. Although the FTC attempted to show a national market for large customers and regional markets for smaller customers, the court found that the regional markets were not sufficiently defined at trial. *Id.*

127. *See id.* at 45-46.

128. *See id.* at 47.

differentiation between the four distribution channels and that the wholesale distribution market was the relevant product market in which to assess the likely competitive effects of the proposed mergers.[129]

Once the relevant market was defined as pharmaceutical wholesalers in the United States, defendants' market dominance allowed the court to find that the FTC had made a *prima facie* case that the proposed merger would have noncompetitive effects in the relevant market.[130] Although this case represents a second recent enforcement victory for the FTC, the court's analysis of the relevant product market is particularly instructive for antitrust practitioners.

3. Virtual Mergers.—In early 1998, the FTC commenced an antitrust investigation of a joint operating agreement between the recently merged two-hospital system—Cross River HealthCare in Kingston, New York and Northern Duchess Hospital in Reinbeck, New York.[131] Additionally, on February 10, 1998, New York Attorney General Dennis Vacco challenged a joint operating agreement between 317-bed St. Francis Hospital and 257-bed Vassar Brothers Hospital, the only acute care facilities in Poughkeepsie, New York.[132] The question of economic integration was raised in both situations.

The U.S. Supreme Court had analyzed economic integration for purposes of antitrust violations and focused on the unity of economic interest of a parent and its wholly owned subsidiary and the inherent control a parent has over subsidiaries.[133] As a general rule, antitrust risks are minimized when (a) the purpose and effect of the joint venture is to facilitate procompetitive efficiencies, (b) the competitive restrictions within the venture are necessary to achieve those efficiencies, and (c) the restraints do not "spill over" to competitor activities outside of the joint venture.[134]

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129. *Id.* at 53-54.

130. *Id.* at 61.

131. *Id.* at 41 n.4.

132. *See id.*

133. Copperweld Corp. v. Independence Tube Co., 467 U.S. 752, 771 (1984). The *Copperweld* doctrine has been expanded to cover agreements between wholly owned subsidiaries of a common parent corporation, *see, e.g.*, Advanced Health-Care Servs., Inc. v. Radford Community Hosp., 910 F.2d 139, 146 (4th Cir. 1990), and to associations of independent entities that exemplify a sufficient unity of economic interest, *see, e.g.*, City of Mount Pleasant, Iowa v. Associated Elec. Coop., Inc., 838 F.2d 268, 275 (8th Cir. 1988) (finding that an electric cooperative and constituent members were single entity); Proctor v. General Conference of Seventh-Day Adventists, 651 F. Supp. 1505, 1523 (N.D. Ill. 1986) (applying the *Copperweld* doctrine to unincorporated church associations that had unity of interest with centralized unified church). For an excellent article summarizing the scope of the *Copperweld* doctrine, see Stephen Calkins, Copperweld *in the Courts; The Road to* Caribe, 63 ANTITRUST L.J. 345 (1995).

134. *Compare* Broadcast Music, Inc. v. Columbia Broadcasting Sys., 441 U.S. 1 (1979) (blanket copyright license for musical compositions was not a per se violation of antitrust laws because the price-fixing was necessary to market the product), *with* Arizona v. Maricopa County Med. Society, 457 U.S. 332 (1982) (price fixing of maximum prices for health services was per se illegal).

Competitor collaborations such as virtual mergers, joint operating agreements, and other affiliations raise significant antitrust concerns if not structured properly. It is likely that the government enforcement agencies will continue to give close scrutiny to merger-like affiliations among healthcare providers.

G. Labor/Employment

The U.S. Supreme Court recently expanded the reach of the Americans with Disabilities Act of 1990 ("ADA")[135] by holding that the human immunodeficiency virus ("HIV") can be a disability under the ADA even when the infection has not yet progressed to the so-called symptomatic phase.[136] The logical outreach of this holding is that employers must reasonably accommodate HIV-infected employees under most circumstances.

In *Bragdon v. Abbott*,[137] the Court utilized a three-step analysis to reach this conclusion.[138] First, the Court concluded that HIV infection is a physical impairment from the moment of infection.[139] In making this determination, the Court largely considered the predictable and unalterable course of the disease, and the immediacy with which the disease begins its course.[140] Second, the Supreme Court concluded that reproduction is a major life activity.[141] To arrive at this conclusion, the Court utilized a common-sensical approach, concluding that reproduction and the sexual dynamic surrounding reproduction are "central to the life process itself."[142] Finally, the Court concluded that a person's HIV infection substantially limits the major life activity of reproduction.[143] The Court pointed to the relative risks of transmitting the virus to sexual partners during conception and the risk to unborn children.[144]

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135. 42 U.S.C. §§ 12101-213 (1994 & Supp. II 1996).

136. Bragdon v. Abbott, 118 S. Ct. 2196 (1998). While this case was actually decided with particular emphasis placed on Title III of the ADA, which prohibits disability in the provision of public accommodations, the implication of the Supreme Court decision also applies to Title I of the ADA, which prevents disability discrimination in employment. The definition of "disability" is the same under both titles. *See id.* at 2209; *see also* 42 U.S.C. § 12102(2) (1994). The ADA defines "disability" as "(A) a physical or mental impairment that substantially limits one or more of the major life activities of such individual; (B) a record of such an impairment; or (C) being regarded as having such an impairment." 42 U.S.C. § 12102(2).

137. 118 S. Ct. 2196 (1998).

138. *Id.* at 2209-10.

139. *Id.* at 2204.

140. *Id.* at 2203-04.

141. *Id.* at 2205. The federal regulations implementing the ADA define "major life activity" as "functions such as caring for oneself, performing manual tasks, walking, seeing, hearing, speaking, breathing, learning and working." 29 C.F.R. § 1630.2(f) (1998).

142. *Bragdon*, 118 S. Ct. at 2205.

143. *Id.* at 2209.

144. *Id.* at 2206.

The Court did not determine whether HIV infection is a per se disability under the ADA.[145] Rather, each individual plaintiff must show that HIV infection substantially limited a major life activity.[146] Favoring a case-by-case approach, the Court left open the scope of "major life activity."[147] The expansive implications of this decision have not yet been analyzed in determining the future interpretation of the definition of a disability under the ADA.

II. INDIANA DEVELOPMENTS

A. Judicial Opinions

In *Creasy v. Rusk*,[148] the Indiana Court of Appeals examined the issue of whether a patient institutionalized in a long-term care facility for the treatment of Alzheimer's disease owes a duty to refrain from conduct which will injure his or her caregivers.

Mr. Rusk was admitted to Brethren Healthcare Center ("BHC") in July 1992 with a primary diagnosis of Alzheimer's disease. At the time of his admission, Mr. Rusk's symptoms included memory loss and confusion, and his wife was unable to care for him at home. Mr. Rusk was known to hit staff members while they attempted to care for him.[149]

Ms. Creasy was a certified nursing assistant, employed by BHC, whose duties required her to care for patients with Alzheimer's disease. Ms. Creasy was aware of the pathological effects of Alzheimer's and had worked with Alzheimer's patients on a regular basis for a number of years prior to the incident in question.[150] On May 16, 1995, Nurse Creasy sustained personal injuries when she was kicked several times by Mr. Rusk while attempting to put the patient to bed. The trial court granted Mr. Rusk's motion for summary judgment, concluding that the patient did not owe a duty to his caretaker, the caretaker incurred the risk of her injuries, the caretaker's comparative fault exceeded all other fault proximately contributing to her injuries, and the caretaker had failed to bring forth evidence that the patient had breached any duty owed to her.[151]

The Indiana Court of Appeals reversed the trial court's decision concluding that "a person's mental capacity, whether that person is a child or an adult, must be factored into the determination of whether a legal duty exists."[152] In its analysis of whether a person institutionalized with a mental disability owes a duty to his caregiver to refrain from conduct that results in injury to the caregiver, the appellate court declined to adopt the general rule which provides

145. *Id.* at 2207.
146. *Id.*
147. *Id.* at 2205.
148. 696 N.E.2d 442 (Ind. Ct. App. 1998).
149. *See id.* at 443.
150. *See id.* at 444.
151. *See id.*
152. *Id.* at 446.

for a different standard of care for adults than for children. Instead, the court reasoned that a person cannot be drawn into a legal relationship with another unless such person is capable of apprehending and appreciating the peril of the situation; thus, a person's mental capacity, whether that person is a child or an adult, must be factored in the determination of whether a legal duty exists.[153] The court further found that while the determination of the existence of a legal duty is generally a question of law, there may be instances in which there are genuine issues of material fact regarding the relationship and foreseeability factors, which "[make] the existence of duty a mixed question of law and fact, ultimately to be decided by the finder of fact."[154]

The appellate court held that "[i]n the absence of extenuating circumstances, the relationship between a patient in a healthcare facility and the caregivers working in the facility is sufficient upon which to base a legal duty."[155] However, the patient's mental capacity to control his actions and understand the consequences thereof may serve to alter the patient-caregiver relationship.[156] "The greater the degree of the patient's impairment, the less weight to be given to the relationship factor in determining legal duty."[157] Furthermore, the court held that "[i]t is foreseeable that when an Alzheimer's patient becomes combative in the presence of his caregiver, the caregiver will be injured."[158]

In *McConnell v. Porter Memorial Hospital*,[159] the Indiana Court of Appeals addressed whether an incident report filed by an employee of a hospital provides sufficient notice to comply with the state's statute governing notice of tort claims against a political subdivision.[160] Dr. McConnell, an emergency room physician, injured his left knee when he slipped and fell on a wet floor in the emergency room. Dr. McConnell was employed by the defendant hospital and filed an incident report regarding the fall. This incident report contained information concerning "the identity of the injured party, the date, a description of the event, diagnostic studies and treatment, and witnesses to the event."[161] Approximately two years after this incident occurred, Dr. McConnell filed a lawsuit against the defendant hospital. The trial court granted the hospital's motion for summary judgment on the basis that Dr. McConnell had not complied with the statutory notice requirements of the Indiana Tort Claims Act.[162]

Upon appeal, Dr. McConnell argued that he had substantially complied with the provisions of the Tort Claims Act by his filing of the incident report with the hospital. The court disagreed, stating that "[n]othing in either the Incident

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153. *Id.*
154. *Id.* (citing State v. Cornelius, 637 N.E.2d 195, 198 (Ind. Ct. App. 1994)).
155. *Id.*
156. *See id.*
157. *Id.*
158. *Id.*
159. 698 N.E.2d 865 (Ind. Ct. App. 1998).
160. *Id.* at 867.
161. *Id.*
162. *See id.*

Report or the Incident Analysis Report placed the hospital on notice that the McConnells intended to present a tort claim."[163] The court also rejected the McConnells' argument of substantial compliance, reiterating the long-standing principle "that negligence will not be presumed or inferred from the mere fact of an accident or injury."[164] The requisite notice to a political subdivision must include not only the fact that an accident has occurred, but also notice that the accident victim intends to assert a tort claim.[165]

In *Doe v. Methodist Hospital*,[166] the Indiana Supreme Court declined to recognize a distinct tort for the public disclosure of private facts or allow such a claim to form the basis of a civil action in Indiana.[167] Mr. Doe was a letter carrier for the United States Postal Service. In early 1990, he was rushed from his workplace to a local hospital via ambulance due to a suspected heart attack. During this transfer, Mr. Doe informed the emergency personnel that he had tested positive for the human immunodeficiency virus ("HIV"). This information was then recorded in Mr. Doe's medical records.[168]

During Mr. Doe's hospitalization, a coworker's wife who was employed by the hospital discovered Mr. Doe's HIV-positive status and disclosed this information to her husband. The coworker then relayed this information to other coworkers, and Mr. Doe alleged that he suffered "embarrassment, humiliation and mental distress" as a result.[169]

The trial court granted defendant's motion for summary judgment. The plaintiff appealed and the court of appeals affirmed.[170] The Supreme Court thereafter granted plaintiff's petition for transfer. Chief Justice Shepard wrote a lengthy history regarding the invasion of privacy tort and its evolution, which is now codified in the Restatement (Second) of Torts.[171] Under the Restatement view, there is a complex of four distinct injuries resulting from the invasion of privacy: (1) intrusion upon seclusion, (2) appropriation of likeness, (3) public disclosure of private facts, and (4) false-light publicity.[172] The court clarified that, although it has generally recognized breach of privacy as an actionable offense, it has never specifically addressed whether the public disclosure of private facts will be a sufficient basis for such an action in Indiana.[173]

In its analysis, the court held that the truth-in-libel provision of the Indiana Constitution suggests "a very strong policy" against the imposition of civil

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163. *Id.* at 868.
164. *Id.* at 869.
165. *See id.*
166. 690 N.E.2d 681 (Ind. 1997).
167. *Id.* at 682.
168. *See id.* at 683.
169. *Id.*
170. *See id.* at 684.
171. *Id.*
172. *Id.* (quoting RESTATEMENT (SECOND) OF TORTS § 652a (1965)).
173. *Id.* at 685.

liability based upon the dissemination of truthful information.[174] Additionally, Chief Justice Shepard reasoned that Indiana law already provides a remedy for the intentional infliction of emotional distress ("outrage") and that emotional injuries sustained by reason of the public disclosure of private facts should not be treated differently from other emotional injuries.[175]

Chief Justice Shepard applied the Restatement's disclosure analysis.[176] Under this analysis, a person is subject to liability for public disclosure of private facts if he or she: "(1) gives 'publicity,' (2) to a matter that (a) concerns the 'private life' of another; (b) would be 'highly offensive' to a reasonable person; and (c) is not of legitimate public concern."[177] The court determined that the coworker's disclosures to a small group of people did not constitute "publicity" as required under the analysis, stating that "[t]he Restatement explicitly observes that communication to a single person or even a small group of persons is not actionable."[178] Instead, "publicity" requires either the communication of the private information to "the public at large, or to so many persons that the matter must be regarded as substantially certain to become one of public knowledge."[179]

In *Ley v. Blose*,[180] the Indiana Court of Appeals held that medical records maintained by hospitals regarding a defendant physician's alcoholism were not protected from discovery in a medical malpractice action.[181] Between 1980 and 1993, Mr. Blose sought and received medical treatment from Dr. Ley for various urological problems and conditions. The plaintiff subsequently filed his complaint against Dr. Ley alleging that, as a result of the defendant physician's negligence, he was denied the benefit of early diagnosis and prompt intervention of a cancerous condition. Both prior and subsequent to the events in dispute, Dr. Ley received treatment for alcoholism and depression. Moreover, in 1995, Dr. Ley surrendered his license to practice medicine.[182]

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174. *Id.* at 687. The Indiana Bill of Rights contains the following provision: "In all prosecutions for libel, the truth of the matters alleged to be libelous may be given in justification." *Id.* (quoting IND. CONST. art. I, § 10).

175. "To establish liability for outrage, a plaintiff must prove that a defendant (1) engaged in 'extreme and outrageous' conduct that (2) intentionally or recklessly (3) caused (4) severe emotional distress." *Id.* at 691 (quoting RESTATEMENT (SECOND) OF TORTS §§ 46 (1965)).

176. *Id.* at 692.

177. *Id.* (quoting RESTATEMENT (SECOND) OF TORTS § 652D & cmt.a (1965)).

178. *Id.*

179. *Id.* In a concurring opinion, Justice Dickson criticized the majority for raising the constitutionality issue sua sponte and stated that Indiana courts have long recognized the tort of public disclosure of private facts in the past, and thus disagreed with the plurality's conclusion that the Indiana Constitution presents a considerable obstacle to the recognition of this tort. However, Justice Dickson agreed that the facts of this case did not establish the requisite "publicity" element of the tort, and thus believed that the transfer should have been denied or the decision of the court of appeals summarily affirmed. *Id.* at 693-95 (Dickson, J., dissenting).

180. 698 N.E.2d 381 (Ind. Ct. App. 1998).

181. *Id.* at 384-85.

182. *See id.* at 382.

During the course of the litigation, Mr. Blose's attorney obtained an order from the trial court directing certain third-party health care providers to release medical records relating to Dr. Ley's treatment for alcohol abuse.[183] Dr. Ley presented an interlocutory appeal, challenging the trial court's order requiring disclosure.

Dr. Ley further contended that his treatment records were protected from disclosure pursuant to the physician-patient privilege as codified in section 34-1-14-5(3) of the Indiana Code.[184] The court confirmed that the Indiana physician-patient privilege normally extends solely to physicians and does not apply to hospitals and other health care facilities, and thus affirmed the trial court's order requiring the disclosure of patient records by various institutional health care providers.[185] However, the court went on to reverse the trial court's decision requiring the disclosure of medical records by the defendant's treating physician, reasoning that "[u]nlike a personal injury plaintiff, Ley did not voluntarily place his physical or mental condition at issue."[186] Furthermore, the defendant physician neither asserted alcoholism as an affirmative defense nor disclosed any specific details about his communications with his treating physician; but instead, he affirmatively opposed disclosure of the medical records. Accordingly, the court concluded that Dr. Ley had not waived his patient-physician privilege, and thus, disclosure of the treating physician's records was prohibited.[187]

Finally, Dr. Ley claimed that certain health care facilities treated him for both alcoholism and depression; thus, he argued, the medical records regarding his treatment at such facilities should be protected as "mental health records."[188] The court agreed that the medical records from these facilities were privileged "to the extent that they pertain[ed to the defendant's] depression," but were not privileged "to the extent that they relat[ed to the diagnosis and treatment of the defendant's] alcoholism."[189]

In *Sanders v. State Family and Social Services Administration*,[190] the Indiana Court of Appeals determined that an applicant for Medicaid assistance must meet the eligibility standards for supplemental security income ("SSI") benefits before she is allowed to "spend-down" her resources to become eligible for Medicaid

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183. *See id.*

184. *See id.* at 383. Indiana Code section 34-1-14-5(3) provides that physicians are not competent witnesses "as to matters communicated to them, as such, by patients, in the course of their professional business, or advice given in such cases." *Id.* (citing IND. CODE § 34-1-14-5(3) (recodified at IND. CODE § 34-46-3-1 (1998))).

185. *Id.*

186. *Id.* at 384.

187. *Id.*

188. *See id.*

189. *Id.* "[I]f the portions of the records pertaining to depression are not facially distinguishable from the portions regarding alcoholism, the records may not be disclosed." *Id.* at 384 n.3.

190. 696 N.E.2d 69 (Ind. Ct. App. 1998).

benefits.[191] Ms. Sanders filed an application for Medicaid benefits with the Wabash County Department of Family and Children requesting Medicaid coverage from August 1995. After examining Ms. Sanders' resources and income, the Family and Social Services Administration ("FSSA") concluded that her resources exceeded the Medicaid eligibility limits. The FSSA further determined that Ms. Sanders did not meet the eligibility requirements for the SSI program and, therefore, could not use the "spend-down" provision to apply her incurred medical expenses to offset her excess resources. Consequently, the FSSA denied Ms. Sanders' application for Medicaid for the reason that her resources exceeded the allowable Medicaid resource limit.[192] Ms. Sanders contended the FSSA's requirement that she first meet SSI eligibility standards before "spending down" her excess income as permitted under Indiana's Medicaid Regulations was unreasonable, arbitrary and capricious, and not otherwise in accordance with federal and Indiana law.

To qualify for Medicaid in Indiana, an applicant must meet both an income eligibility test and a resource eligibility test. Under certain circumstances, an applicant may be allowed to "apply his incurred medical expenses as a setoff against his excess resources for the relevant period. . . . However, 'Indiana did not intend to extend Medicaid eligibility to those who would not even qualify for benefits under SSI's more liberal requirements, because it did not endorse the more restrictive eligibility requirements by opting for 209(b).'"[193] Consequently, the resource spend-down component enabling eligibility for Medicaid "applies only after [the less restrictive] SSI eligibility requirements have been met."[194] The court thus concluded that because Ms. Sanders did not meet the eligibility criteria for SSI benefits, FSSA properly determined that she was not entitled to apply her incurred medical expenses as a setoff against her excess resources in order to become eligible for Medicaid assistance.[195]

In *State Family & Social Services Administration v. Thrush*,[196] the Indiana Court of Appeals considered whether the "first day of the month" rule for calculating a Medicaid applicant's resources is arbitrary and capricious in situations where the applicant's unliquidated assets have already been applied to offset the applicant's unpaid medical bills in prior months.[197] Mrs. Thrush was hospitalized for approximately five months before her death. As a result of this hospitalization, her husband filed an application seeking Medicaid assistance for the payment of her medical bills which exceeded $180,000. Mr. Thrush was advised that his assets exceeded the Medicaid eligibility limits and thus, he was required to "spend down" his excess resources in order to qualify for Medicaid

191. *Id.* at 72.

192. *See id.* at 70.

193. *Id.* at 71 (quoting Department of Pub. Welfare v. Payne, 622 N.E.2d 461, 463 n.1, 468 (Ind. 1993)).

194. *Id.* at 71-72.

195. *Id.* at 72.

196. 690 N.E.2d 769 (Ind. Ct. App. 1998).

197. *Id.* at 770.

assistance. Mr. Thrush acknowledged that his assets exceeded the eligibility limit; however, he disputed the county's calculation of his required spend-down amounts.[198]

Mr. Thrush appealed the county's decision to an administrative law judge ("ALJ") and, following an evidentiary hearing, the ALJ affirmed the agency's decision, which was later adopted by FSSA. Mr. Thrush filed a petition for judicial review, whereupon the trial court affirmed FSSA's determination with regard to one month but concluded that FSSA erred in its calculation of the spend-down amount for three subsequent months and remanded the matter for further proceedings. The FSSA appealed.[199]

Medicaid applicants must meet both an income eligibility test and a resources eligibility test. In Indiana, an applicant's financial resources are evaluated on the first day of each month for which Medicaid assistance is sought.[200] "If the applicant's financial resources exceed the eligibility limit on the first day of the month, then the applicant is not eligible for that month."[201] However, an applicant whose financial resources exceed the eligibility limit on the first day of the month may still qualify for Medicaid assistance by "spending down" or off-setting his excess resources against incurred but unpaid medical bills.[202]

The Indiana Court of Appeals clarified that the purpose of the spend-down provision is to encourage Medicaid applicants to use available resources to pay their outstanding medical obligations. Medicaid is not responsible for the portion of an applicant's medical expenses that the applicant could have paid through his own income and resources had he chosen to do so. Accordingly, the court concluded that the first day of the month rule is consistent with the underlying purposes of the Medicaid program and is not inherently unreasonable, nor was the rule applied to *Thrush* in a manner that was arbitrary, capricious, an abuse of discretion, or otherwise contrary to law.[203]

In *Board of Trustees of Knox County Hospital v. Shalala*,[204] the Seventh Circuit upheld the Health and Human Services ("HHS") policy of relying exclusively on the agency's own published data to determine the case mix index ("CMI") of a provider seeking to qualify as a rural referral center ("RRC").[205] Good Samaritan Hospital is a 342-bed acute care facility which offers many services comparable to major urban hospitals and therefore sought to be

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198. *See id.* at 771.

199. *See id.*

200. *See id.* at 772. "[T]he 'first day of the month' rule . . . which provides in relevant part: (a) [a]n applicant or recipient is ineligible for medical assistance for any month in which the total equity value of all nonexempt personal property exceeds the applicable limitation set forth below, on the first day of the month . . . ." *Id. See* IND. CODE § 12-15-2-1 (1998).

201. *Thrush*, 690 N.E.2d at 772 (citing Glaser v. Department of Pub. Welfare, 512 N.E.2d 1128, 1132 (Ind. Ct. App. 1987)).

202. *See id.* (citing Department of Pub. Welfare v. Payne, 622 N.E.2d 461 (Ind. 1993)).

203. *Id.*

204. 135 F.3d 493 (7th Cir. 1998).

205. *Id.*

designated as a RRC beginning in the 1985 fiscal year for services rendered to Medicare beneficiaries, the Board of Trustees of Knox County Hospital d/b/a Good Samaritan Hospital ("Good Samaritan"). Under such a designation, the hospital would be entitled to reimbursement at the higher payment rate for urban areas despite its rural location.[206] It is undisputed that Good Samaritan met three of the four requirements required for RRC statutes provided at 42 CFR sections 405 and 476(a)(1)(iii). However, the parties dispute whether Good Samaritan satisfied the remaining requirement based upon the hospital's 1981 CMI.[207]

Specifically, a provider is eligible for RRC status if its 1981 CMI equals or exceeds 1.1053.[208] The Secretary of HHS (the "Secretary") had calculated Good Samaritan's 1981 CMI based upon CMI's own statistical file that consisted of information concerning only twenty percent of Good Samaritan's 1981 Medicare discharges. Good Samaritan had retained a nationally-recognized consulting firm, the Commission of Professional Hospital Activities ("CPHA"), to recalculate its 1981 CMI. CPHA's recalculation, based upon a study of one hundred percent of Good Samaritan's 1981 Medicare discharges, determined that the provider's 1981 CMI was actually 1.0637. Good Samaritan appealed the agency's decision to the Provider Reimbursement Review Board ("PRRB"), which ruled that the hospital had satisfied the eligibility criteria to qualify for RRC status.[209] The Secretary, acting through the administrator of HCFA, thereafter reversed the PRRB's decision and Good Samaritan then appealed the Secretary's decision to the U.S. District Court. The court entered summary judgment in favor of the Secretary, holding that the Secretary "'did not act in a manner which was arbitrary and capricious, an abuse of discretion, or contrary to law when she determined that Good Samaritan's CMI did not satisfy the regulatory requirement.'"[210] This appeal ensued.

Good Samaritan contended that the Secretary's interpretation of the RRC statute is inconsistent with its statutory language and basic purpose because the RRC statute grants a health care provider the right to challenge the Secretary's CMI calculation. The hospital thus argued that the Secretary's refusal to allow the substitution of CPHA data in lieu of its own published 1981 case mix index is arbitrary, capricious, and contrary to law. The Seventh Circuit agreed that the

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206. *See id.* at 496-97.

207. There are actually three alternate sets of criteria under which a provider could qualify as a RRC. Good Samaritan sought eligibility based upon the third test, which requires that the provider be located in a rural area, meet or exceed certain mandatory discharge criteria, and satisfy certain criteria pertaining to the composition of the hospital's medical staff and inpatient population. Additionally, the hospital is required to satisfy any one of four CMI criteria; one of which provides that "a hospital is eligible for RRC status if its 1981 CMI was equal to or exceeded 1.03." Good Samaritan argued that it met all criteria as set forth in the aforesaid test. *See id.* at 496 (citing 42 C.F.R. § 405.476(g)(1)(iii)(A)(1),(2),(3) &(4)).

208. *See id.*

209. *See id.*

210. *Id.* at 408 (quoting Board of Trustees of Knox County Hosp. v. Shalala, 959 F. Supp. 1026, 1028 (S.D. Ind. 1997)).

Secretary has a substantial interest in using her own published calculations of a provider's 1981 CMI as a basis for determining eligibility for RRC status; and concluded that the Secretary's policy was not arbitrary and capricious.[211]

B. Statutory Developments

1. Creation of Children's Health Insurance Program ("CHIP").—Effective September 1, 1998, the Indiana General Assembly authorized a new program for health insurance coverage for children meeting certain family income eligibility standards. Senate Enrolled Act 19,[212] which established an Indiana program in accordance with provisions of the federal Balanced Budget Act of 1997,[213] enables the state to use up to $70 million in federal funds with approximately $26 million in state funds,[214] to provide health insurance coverage for children whose family's income does not exceed one hundred and fifty percent of federal poverty standards.[215] An expansion of eligibility in the existing Indiana Medicaid Program provides such coverage. The statute also requires the Office of Medicaid Planning and Policy ("OMPP") to expend the maximum amount of authorized federally provided funds in outreach activities designed to inform and enroll eligible beneficiaries.[216] Family and Social Services Administration ("FSSA") is required to develop and implement a presumptive eligibility program consistent with federal guidelines for CHIP programs.[217] Presumptive eligibility allows a child or pregnant woman to begin to receive services based on an analysis of preliminary information that indicates eligibility prior to formal determination of eligibility.[218] To ensure reasonable access to enrollment and services, a disproportionate share provider, a federally qualified health center, or a rural clinic are acceptable entities to determine presumptive eligibility.[219] Effective July 1, 1999, an Office of the Children's Health Insurance Program within the Office of the Secretary of FSSA will oversee the provision of health services for eligible children.[220]

The act also provides twelve months of continuous Medicaid coverage to all Medicaid-eligible children on September 1, 1998 regardless of whether the child's family's income exceeds one hundred and fifty percent of the federal poverty level during the succeeding twelve month period.[221] This provision will allow beneficiaries to receive appropriate continuity of care irrespective of

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211. *Id.* at 499-500.
212. S. 19, 110th Legis., 2d Sess. (Ind. 1998).
213. 42 U.S.C. § 1396d(u) (1994 & Supp. II 1996).
214. *See id.*
215. *See* IND. CODE § 12-15-2-15.6(a)(1) (1998).
216. *Id.* § 12-15-1-18.
217. *See id.* § 12-15-2.2-1.
218. *See id.*
219. *See id.*
220. *See id.* § 12-17-18-1.
221. *Id.* §12-15-2-15.7(a).

fluctuations in income. Senate Enrolled Act 19, in creating the Indiana CHIP program, is a significant program for identifying and providing health care services to children.

2. Changes in Indiana Medicaid Disproportionate Share ("DSH") Hospital Payment Program.—House Enrolled Act 1349 ("Act 1349")[222] substantially restructures the Indiana Medicaid DSH Program and creates additional programs allowing increased Medicaid payments to eligible municipal hospitals, government-owned hospitals that have "Medicaid shortfalls,"[223] and community mental health centers.[224] Further, the Act modifies the existing Hospital Care for the Indigent Program ("HCI") by permitting increased Medicaid payments to hospitals located in counties whose county HCI tax levies paid to the state exceed payments made to providers of HCI services within the county.

The basic DSH program is continued and Act 1349 allows a hospital to obtain Medicaid basic DSH payments if the hospital's Medicaid inpatient utilization rate is at least one standard deviation above the mean Medicaid inpatient utilization rate for all Indiana hospitals, or if a hospital's low-income utilization rate exceeds twenty-five percent of total utilization.[225] Payment to eligible basic DSH hospitals is based on a formula involving calculation of Medicaid day utilization, discharge rates, and total patient days based on the type of eligible hospital and on information from the most recent year for which audited data is available.[226]

The enhanced DSH program is extended in Act 1349 and eligibility is modified.[227] This program is dependent upon intergovernmental transfers of money from certain government-owned hospitals to the state, which allows the state through the OMPP to obtain a federal match for the funds if expended as Medicaid payments.[228] The program permits additional hospitals to receive enhanced DSH payments in state fiscal year 1998 and thereafter based on annual updates of Medicaid inpatient utilization rates and low-income utilization rates.[229] Payments to eligible hospitals will be based upon a formula that limits total payments to the sum of a hospital's total expenditure for charity care and Medicaid shortfall.

Municipal hospitals are now specifically eligible to participate in a new DSH program if the hospital meets a minimum standard of Medicaid utilization[230] and voluntarily makes an intergovernmental transfer of money to the state, allowing OMPP to obtain a federal match of the funds if expended as Medicaid

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222. H. 1349, 110th Legis., 2d Sess. (Ind. 1998).
223. IND. CODE §12-15-18-5.1 (1998).
224. *Id.* § 12-15-19-9.
225. *Id.* § 12-15-16-1(a).
226. *See id.* §§ 12-15-16-1(f), 2.
227. *Id.* § 12-15-19-1.
228. *See id.* § 12-15-19-8.
229. *See id.* §12-15-18-5.1(a).
230. *See id.* § 12-15-19-8.

payments.[231] Participating hospitals will receive additional Medicaid payments equaling amounts transferred to the state plus an additional amount to partially offset charity care expenditures of the hospital. OMPP will retain part of the money obtained from the federal match and will transfer the remainder to the Medicaid indigent care trust fund to be paid out to basic and enhanced DSH eligible hospitals.[232]

Act 1349 states that, effective state fiscal year 1998, government-owned hospitals that have Medicaid shortfalls, which is the difference between its Medicaid payments and its Medicare upper payment limit, may receive additional Medicaid payments if the hospital voluntarily makes an intergovernmental transfer of money to the state.[233] This allows OMPP to obtain a federal match of the funds if expended as Medicaid payments.[234] Participating hospitals will receive additional Medicaid payments equaling amounts transferred to the state plus an additional amount to partially offset the hospital's Medicaid shortfall. OMPP will retain part of the money obtained from the federal match and transfer the remainder to the Medicaid indigent care trust fund to be paid out to basic and enhanced DSH eligible hospitals.[235]

Act 1349 also established a program authorizing additional Medicaid payments for eligible community mental health centers ("CMHC").[236] To be eligible, a CMHC must own and operate an inpatient care unit, must receive payments from a political subdivision, and have a Medicaid inpatient utilization rate of at least one percent during the most recent state fiscal year.[237] In counties with CMHCs meeting the eligibility requirements, the county treasurer must certify that funds were paid to the eligible CMHC.[238] The certification then serves as the equivalent of the state's share of a Medicaid payment, which permits a federal match of the certified amounts.[239] OMPP, upon receipt of the federal match, will make an additional Medicaid payment to the eligible CMHC equal to the federal match.[240]

3. *Managed Care Consumer Protection.*—In response to constituent complaints and consumer activism, the legislature enacted Senate Enrolled Act 364 ("Act 364").[241] Act 364 requires health maintenance organizations ("HMO"s) to make annual reports to the Indiana Department of Insurance specifying the number of providers credentialed by the HMO that meet current standards of the National Committee on Quality Assurance and providing

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231. *See id.* § 12-15-15-1.1.
232. *See id.* § 12-15-19-8.
233. *Id.* § 12-15-18-5.1.
234. *See id.*
235. *See id.* § 12-15-15-1.1.
236. *Id.* § 12-15-18-5.1.
237. *See id.* § 12-15-16-1(d).
238. *See id.* § 12-15-18-5.1(e).
239. *See id.*
240. *See id.* § 12-29-1-7.
241. S. 364, 110th Legis., 2d Sess. (Ind. 1998).

information on the HMO's Health Plan Employer Data and Information Set.[242] It also requires HMOs to provide coverage and payment for services provided in hospital emergency rooms, irrespective of prior authorization or an existing contractual relationship between the HMO and provider if a prudent lay person could reasonably believe the enrolled patient's condition required immediate medical attention.[243] HMOs must pay for these services at the usual, customary and reasonable charge for the same services in the HMO's service area or an amount agreed to between the HMO and provider.[244] HMOs are also required to appoint medical directors who are licensed physicians[245] and to stipulate in contracts with providers that if the contract is terminated for reasons other than inadequate quality, the provider must continue to care for assigned enrollees up to sixty days following termination of the contract.[246] Act 364 further requires that the HMO have sufficient providers to meet enrollee needs and afford a choice of providers.[247] In addition, HMOs must also maintain telephone access during business hours for routine care and twenty-four hour access for required prior authorization of care.[248] Enrollees are entitled to reasonable access to appointment schedules in accord with HMO guidelines.[249]

If an HMO enrollee requires a covered service not available through the HMO's existing providers, the HMO must refer the enrollee to another provider and pay for the services rendered.[250] An HMO must offer another choice of provider,[251] point-of-service option to purchasers,[252] and second opinion option for enrollees.[253] Any HMO formulary for drugs and Medicaid devices must be developed by a committee composed of a majority of licensed physicians, must be disseminated to participating providers and pharmacists, and must provide for an expeditious process for enrollees to obtain non-formulary drugs.[254] Every HMO must also establish and maintain a drug utilization review program.[255] HMOs are required to develop and implement procedures to evaluate provision of coverage to an enrollee for new technologies, treatments, procedures, drugs, and devices.[256]

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242. IND. CODE § 27-13-8-2(a)(4), (5) (effective Jan. 1, 2000).
243. *Id.* § 27-13-36-9(c) (1998).
244. *See id.* § 27-13-36-9(d).
245. *See id.* § 27-13-36-1(a).
246. *See id.* § 27-13-36-6.
247. *Id.* § 27-13-36-2.
248. *See id.* § 27-13-36-7.
249. *See id.* § 27-13-36-8.
250. *See id.* § 27-13-36-5.
251. *See id.* § 27-13-37-2.
252. *See id.* § 27-13-37-4.
253. *See id.* § 27-13-37-5.
254. *See id.* § 27-13-38-1.
255. *See id.* § 27-13-38-3.
256. *See id.* § 27-13-39-1(a).

4. *Newborn HIV Testing.*—Senate Enrolled Act 261[257] permits a physician to order a confidential newborn HIV test if a mother of a newborn has not had the test, the mother refuses to consent to the test, and the physician reasonably believes the test is medically necessary.[258] If a physician orders a test, the mother must be notified and provided with appropriate medical information and counseling.[259] Results of an HIV test on a newborn must be provided to the mother.[260] If a parent of the newborn objects in writing to an HIV test on his or her newborn and the objections are based on religious beliefs, the newborn is not required to have the test.[261]

5. *Payments to Mental Health Providers.*—The Division of Mental Health ("DMH") of the Indiana Family and Social Services Administration ("FSSA") is authorized by Senate Enrolled Act 461 ("Act 461")[262] to develop per diem or prospective payment mechanisms for community mental health centers ("CMHC") for some eligible mentally ill and substance abuse patients.[263] Act 461 requires DMH to continue implementation of a specific payment program for CMHCs for the care of seriously mentally ill adults.[264] In developing payment programs, DMH is required to use actuarial principles and generally accepted accounting principles in determining appropriate payment based on efficiently and effectively operated treatment programs for mental health patients.[265]

6. *The Indiana Medical Malpractice Act.*—The 1998 legislative session saw substantial changes to the Indiana Medical Malpractice Act. On March 16, 1998, after unanimously passing in both the House and the Senate, Senate Enrolled Act 390 ("Act 390")[266] was signed into law. Act 390 amended the minimum insurance requirements for health care providers and changed the way in which the health care provider surcharge is calculated. After July 1, 1999, health care providers must have a per occurrence insurance policy which insures to at least $250,000.[267] Similarly, annual aggregates for hospitals and other health care providers will increase and range from $750,000 and $7.5 million.[268]

Act 390 also amended the way in which a provider's surcharge is calculated. Prior to the passage of Act 390, the annual surcharge that insured hospitals paid into the Patient Compensation Fund ("PCF") could not exceed two hundred

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257. S. 261, 100th Legis., 2d Sess. (Ind. 1998).

258. IND. CODE § 16-41-6-4(a).

259. *See id.* § 16-41-6-4(b).

260. *See id.* § 16-41-6-4(d).

261. *See id.* § 16-41-6-4(e).

262. S. 461 Legis., 2d Sess. (Ind. 1998).

263. IND. CODE § 12-21-2-7.

264. *Id.*

265. *See id.*

266. S. 390, 110th Legis., 2d Sess. (Ind. 1998).

267. *See id.* This is a change from a per-occurrence amount of at least $100,000. *See* IND. CODE § 34-18-4-1.

268. *See* IND. CODE § 34-18-4-1. This is an increase from $300,000 for other providers to up to $3 million for hospitals with greater than 100 beds.

percent of its insurance premium.[269] Self-insured hospitals were required to pay an amount equal to one hundred and fifty percent of the premium that would have been charged to the provider by the Residual Malpractice Insurance Authority.[270]

After July 1, 1999, the surcharge for hospitals will be determined by taking information generated by the hospital and feeding that information into an actuarial program created by the Indiana Department of Insurance, which will determine the actuarial risk posed to the patient compensation fund by a hospital.[271] The program must take into consideration risk management programs used by the hospital, be an efficient and accurate means of calculating a hospital's actuarial risk, be publicly identified by the Indiana Department of Insurance by July 1 of each year, and be made available to the hospital's malpractice carrier to calculate the hospital's surcharge.[272]

A new surcharge formula was also created for physicians, which de-couples the surcharge payment from the insurance premium. Now, each year the insurance commissioner must contract with an actuary to determine the risk physicians pose to the PCF.[273] The actuary will calculate the average of the three leading malpractice insurers' actual rates for all physicians practicing in the same specialty class or discipline. Using that information, the actuary will establish a uniform charge for all physicians practicing in the same specialty.[274] Other providers will be assessed an annual surcharge of one hundred percent of its insurance premium.[275]

In addition, the legislature passed House Enrolled Act 1011 ("Act 1101"),[276] which repealed Indiana Code section 27-12 and re-enacted the Malpractice Act as Indiana Code section 34-18.[277] The re-enactment brought several changes to Act 1011. What follows is not an exhaustive list of the changes made to the Act, but represents several of the more substantive changes. After July 1, 1999, an insurance policy issued in Indiana must contain a provision that authorizes an insurer to settle a case without the consent of the insured after a medical review panel has issued a unanimous decision finding that the provider deviated from the applicable standard of care.[278] Nothing requires that the medical review panel also find against the healthcare provider on the issues of causation and injury.[279]

The Malpractice Act added Indiana Code section 34-18-8-8, which allows a

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269. *See id.* § 27-12-5-2 (Supp. 1997) (amended 1998).

270. *See id.* § 27-12-5-4 (Supp. 1997) (amended 1998).

271. *See id.* § 34-18-5-2(c) (1998) (effective July 1, 1999).

272. *See id.* § 34-18-5-2(a)(1-4) (1998).

273. *See id.* § 34-18-5-2(f)(1). Under prior Indiana law, the amountof the surcharge paid by a physician was calculated at 150% of the premium paid under the physician's insurance policy.

274. *See id.*

275. *See id.* § 34-18-5-2(b).

276. H. 1011, 110th Legis., 2d Sess. (Ind. 1998).

277. IND. CODE §§ 34-18-1-1 to -18-18-2 (1998).

278. *See id.* § 27-1-13-7(b). Before July 1, 1999, an insurance contract could specify that a physician's consent was required prior to settling a malpractice claim. *Id.*

279. *See id.*

malpractice case filed before the Indiana Department of Insurance to be dismissed if there has been no action taken on the claim for two years or more.[280] The proper forum for filing a dismissal action is the Marion Circuit Court.[281] In addition, after July 1, 1999, plaintiffs may initiate their malpractice claims both with Indiana Department of Insurance and in state court.[282] However, the state court action may not name the defendants, nor may the action be pursued until after a decision has been issued by a medical review panel.[283] The purpose for this addition was simply to hold the plaintiff's place in line on the court docket.

One significant change in the 1998 amendments to the Malpractice Act includes the addition of a provision which requires medical review panels to issue a separate determination as to whether the health care provider in question should undergo a "fitness to practice" review by the appropriate licensing board.[284] If a panel unanimously determines that the provider should undergo a fitness review, the Commissioner of the Department of Insurance must forward that provider's name to the appropriate licensing agency.[285] However, the panel's determination on the fitness to practice issue is not admissible as evidence in a civil action.[286]

Finally, for acts of malpractice that occur prior to July 1, 1999, an injured party is allowed access to the PCF until the provider (or providers) involved have paid a settlement of at least $75,000.[287] For claims arising after June 30, 1999, this amount has been increased to $187,000.[288] This amendment may see more defendants named in the initial Proposed Complaint to increase the number of providers who could contribute to the potential settlement.

CONCLUSION

Practitioners in the area of health care law must continue to focus on the increased scrutiny by government agencies regarding compliance with the Anti-Kickback Statute, Stark II and other laws. These effects, along with increased pressures to attend to the needs of health care patients in an efficient manner while maintaining quality, will continue to present challenges to those practitioners advising health care clients.

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280. *Id.* § 34-18-8-8. Prior to the addition of this statutory section, there was no provision allowing for the dismissal of a case where there had been no action taken.

281. *See id.*

282. *See id.* § 34-18-8-7.

283. *See id.* The provision does, however, allow a court to set a case for trial prior to the completion of the medical review panel process. *Id.*

284. *Id.* § 34-18-9-4. Prior to this amendment, the Commissioner of Insurance was required to forward a provider's name to the licensing board only when there was a settlement or judgment rendered against the provider.

285. *See id.*

286. *See id.*

287. *See id.* § 34-18-14-4.

288. *See id.*

INDIANA APPELLATE PROCEDURE IN 1998

MICHAEL A. WILKINS*
A. RICHARD M. BLAIKLOCK**

INTRODUCTION

During the survey period,[1] important judicial decisions applicable to appellate procedure were made which must be considered when working on an appeal before Indiana appellate courts. The survey period also marked the time period during which the Indiana Supreme Court implemented significant appellate rule changes.[2] Although the most significant of the 1998 amendments to the Indiana Rules of Appellate Procedure ("Appellate Rule(s)") were those found in Appellate Rule 2(C),[3] there has been no substantive discussion of those amendments in cases reported during the survey period. Of course, other procedural issues were considered by appellate courts during the survey period. Cases that offer insight into the Appellate Rules are addressed in Part I of this Article. Cases dealing with common law principles applicable to appellate procedure are addressed in Part II of this Article. Part III of the Article considers court interpretations of Indiana Trial Rules, to the extent those rules bear on appellate procedure.

I. CASES ADDRESSING THE APPELLATE RULES

A. Appellate Rule 2(A) and Indiana Trial Rules 23(B) and 59(C)

Last year's Article noted that the issue of what constitutes an "appealable final order" within the meaning of Appellate Rule 2(A) and Indiana Trial Rule 59(C) remained unsettled with respect to class action certification orders.[4] The court of appeals had, in *Martin v. Amoco Oil Co.*,[5] addressed the issue of whether a class certification order is a "final appealable order" even if it does not contain the "magic language" from Trial Rule 54(B); namely, an express determination that there "is no just reason for delay," accompanied by an express direction of entry of judgment.[6] In short, the court of appeals sought to revive application of

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* Partner, Ice Miller Donadio & Ryan. B.A., 1985, University of Notre Dame; J.D., 1988, University of Notre Dame.

** Associate, Ice Miller Donadio & Ryan. B.A., 1990, Hanover College; J.D., *summa cum laude*, 1997, Indiana University School of Law—Indianapolis.

1. October 1, 1997, to September 30, 1998.

2. *See*, Michael A. Wilkins & A. Richard M. Blaiklock, *Indiana Appellate Procedure in 1997*, 31 IND. L. REV. 669, 689-94 (1998) (reviewing those appellate rule changes).

3. *See* Wilkins & Blaiklock, *supra* note 2, at 689-91. In Appellate Rule 2(C), the pre-appeal conference has been eliminated and a "Notice of Appeal" filing requirement has been added.

4. *Id.* at 669-72. The procedures for class action certification are found in Indiana Trial Rule 23.

5. 679 N.E.2d 139 (Ind. Ct. App. 1997).

6. *Id.* at 144.

the "definite and distinct branch" doctrine in the context of determining whether a class certification order is a "final appealable order."[7] By attempting to revive the doctrine, the court of appeals created a significant amount of confusion on this issue, an issue that until that time seemingly fell within the purview of the clear language found in *Berry v. Huffman*,[8] in which the Indiana Supreme Court lucidly rejected the "definite and distinct branch" doctrine.[9]

As predicted in this Article last year,[10] the supreme court rejected the position taken by the courts of appeal in *Martin* and *Connerwood Healthcare*, and held that unless the "magic language" of Trial Rule 54(B) is included in a class action certification order, then the order is not automatically considered a "final appealable order" within the meaning of Appellate Rule 2(A) and Indiana Trial Rule 59(C).[11]

Central to the appellate court's analysis in *Martin* was that the ruling in *Berry*—in which the supreme court rejected application of the "definite and distinct branch" doctrine—did not apply to cases deciding motions for certification under Indiana Trial Rule 23, because the *Berry* decision dealt with a motion for partial summary judgment under Indiana Trial Rule 56(C).[12] The supreme court rejected that attempt to distinguish *Berry*, and reaffirmed that *Berry* "addressed the general appealability of orders under Trial Rules 54 and 56."[13] The court then quoted from its *Berry* decision, noting that: "'Judgments or orders as to less than all of the issues, claims, or parties remain interlocutory until expressly certified as final by the trial judge.'"[14] If the definite and distinct branch doctrine still had application in light of the Indiana Trial Rules, "'litigants would . . . be left to guess whether or not a given order was appealable. This [was] precisely the situation that [Trial Rule] 54(B) and 56(C) were drafted and adopted to prevent.'"[15] That "logic applies with equal force to class certification

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7. *Id.* Ultimately the *Martin* court found that the interveners had waived their right to challenge class certification. *Id. See also* Connerwood Healthcare, Inc. v. Estate of Herron, 683 N.E.2d 1322, 1325 n.2 (Ind. Ct. App. 1997).

8. 643 N.E.2d 327 (Ind. 1994).

9. *Id.* at 329.

10. Wilkins & Blaiklock, *supra* note 2, at 672. There, we observe that

> it is predicted that when the Supreme Court considers the issue of whether a class action certification order is a final appealable order, it will decide that unless the "magic language" of Trial Rule 54(B) is included in the order, then the order is not automatically considered a "final appealable order" within the meaning of Appellate Rule 2(A) and Indiana Trial Rule 59(C). Such a result is consistent with the predictability that was at the core of the *Berry* decision, and which is now lost because of the *Connerwood Healthcare* opinion.

Id.

11. Martin v. Amoco Oil Co., 696 N.E.2d 383, 386 (Ind. 1998).

12. *See id.* at 385.

13. *Id.*

14. *Id.* (quoting *Berry*, 643 N.E.2d at 329).

15. *Id.* (quoting *Berry*, 643 N.E.2d at 329).

orders and, indeed, to all orders for judgments which are not 'final' under the requirements of Trial Rule 54(B). Were this not so, the rule would undoubtedly be swallowed by its own exceptions."[16]

The court then set forth a discussion of the genesis and purpose of Trial Rules 54(B) and 56(C):

> We adopted [Trial] Rules 54(B) and 56(C), based on the Federal model, in an effort to provide greater certainty to litigating parties and to strike an appropriate balance between the interests in allowing for speedy review of certain judgments and in avoiding the inefficiencies of piecemeal appeals. Unsatisfactory experiences with the common law "distinct and different branch of litigation" doctrine, which often lead to inefficient and unjust results, had much to do with the change.[17]

Accordingly, the court held that:

> A judgment or order as to less than all of the issues, claims, or parties in an action may become final only by meeting the requirements of Trial Rule 54(B). These requirements are that the trial court, in writing, expressly determine that there is no just reason for delay and, in writing, expressly direct entry of judgment.
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> * * *
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> The formalistic (but bright line) approach to which we now adhere removes uncertainties about when a party should appeal, thus minimizing the risk that an appeal will be dismissed as premature or that the right to appeal will be inadvertently lost. Further, the rules place the discretion of deciding when the facts indicate that a judgment should be deemed final in the hands of the individual best able to make such decisions—the trial judge.[18]

With respect to class action certification rulings in particular, unless a trial court certifies that such a ruling is final under Trial Rule 54(B), "it remains interlocutory."[19] The court thus expressly overruled the decision of the court of appeals to the extent it supported a continuation of the distinct and definite branch doctrine.[20] The court also overruled "other cases" that support continuation of that doctrine,[21] and "specifically disapproved" footnote two of the *Connerwood Healthcare* decision.[22]

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16. *Id. See also id.* ("The distinct and different branch doctrine, superceded by our adoption of the Indiana Rules of Trial Procedure as explicitly stated in *Berry*, would live on in practice if not in word.")
17. *Id.* (citations omitted).
18. *Id.* (citations omitted).
19. *See id.* at 385-86.
20. *Id.* at 385.
21. *Id.*
22. *Id.* at 385 n.3.

With its decision in *Martin*, the supreme court has most likely issued the death knell to the definite and distinct branch doctrine. However, it had seemingly already done so in *Berry*, only to find out that its clear pronouncements on the subject in *Berry* were not clear enough. Fortunately, the supreme court has further removed any uncertainty from the final appealable order issue, even though by doing so it had to subscribe to a "formalistic (but bright line) approach."[23] When it comes to procedural matters, such a formalistic approach should be welcomed by appellate practitioners.

B. Appellate Rule 2(A) and Post-Conviction Rule 2

In *Greer v. State*,[24] the Indiana Supreme Court decided whether "the Court of Appeals has subject matter jurisdiction over a belated appeal from a trial court's denial of credit time following revocation of probation."[25] "Effective January 1, 1994, an amendment to Indiana Post-Conviction Rule 2 [("P-C.R. 2")]created a limited avenue for permitting the filing of a belated praecipe."[26] In short, that amendment "authorizes trial courts to permit the filing of a belated praecipe, but only 'for appeal of [a] conviction.'"[27] In *Greer*, the supreme court strictly construed that exception, stating that:

> The 1994 amendments transformed P-C.R. 2(1) into a "vehicle for belated direct appeals alone." As such, P-C.R. 2(1) provides a method for seeking permission for belated consideration of appeals addressing conviction, but does not permit belated consideration of appeals of other post-judgment petitions. Here, [the defendant] was not appealing his conviction . . . . Instead, [the defendant] was appealing the trial court's denial of credit time following revocation of his probation, which is outside the purview of P-C.R. 2(1). The trial court erroneously permitted [the defendant] to file a belated praecipe.[28]

Accordingly, the supreme court concluded that the amendment to P-C.R. 2(1) did not invest the trial court with jurisdiction to permit the filing of belated praecipes for anything other than direct appeals of convictions.[29] P-C.R. 2(1), as amended, "removes the subject matter of other than direct appeals from the jurisdiction of the [Indiana] Court of Appeals, unless such appeals or petitions are brought pursuant to a timely praecipe."[30]

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23. *Id.* at 385.
24. 685 N.E.2d 700 (Ind. 1997).
25. *Id.* at 701.
26. IND. POST-CONVICTION RULE 2(1).
27. Neville v. State, 694 N.E.2d 296, 297 (Ind. Ct. App. 1998) (quoting IND. POST-CONVICTION RULE 2(1)).
28. *Greer*, 685 N.E.2d at 702 (quoting Howard v. State, 653 N.E.2d 1389, 1390 (Ind. 1995)).
29. *Id.* at 703.
30. *Id.*

It is evident that Indiana's appellate courts will continue to strictly construe Appellate Rule 2(A), even when given the opportunity for wiggle room via some express exceptions to the rule, such as P-C.R. 2(1). Any such exceptions, like Appellate Rule 2(A), will be strictly construed against expanding, or creating uncertainty in, the time period within which to file a praecipe.

C. Appellate Rules 3(A) and 4(B)

In *City of New Haven v. Allen County Board of Zoning Appeals*,[31] the court of appeals revisited the issue of what jurisdiction is retained by a trial court while an interlocutory appeal is pending before the court of appeals. According to Appellate Rule 3(A), "every appeal shall be deemed submitted and the appellate tribunal deemed to have acquired general jurisdiction on the date the record of the proceedings is filed with the clerk of the Supreme Court and the Court of Appeals."[32] In short, "[a]n appeal of a final judgment transfers general jurisdiction of the case to [the court of appeals], thereby suspending any further action by the trial court."[33]

In *City of New Haven*, the City of New Haven (the "City") filed the record of proceedings with the court of appeals relative to an interlocutory appeal.[34] Subsequent to the taking of that interlocutory appeal, other parties to the litigation (all other parties except the City), entered into an agreed judgment that was, after the taking of that interlocutory appeal, certified by the trial court under Indiana Trial Rule 54(B). Before getting into the substantive challenges to entry of that agreed judgment—e.g., that it was "corrupt"—the City challenged entry and certification of that agreed judgment on the grounds that the trial court was without jurisdiction to certify that judgment because the City had initiated its interlocutory appeal, thus divesting the trial court of jurisdiction to enter the agreed judgment.[35]

The court of appeals observed the following with respect to the entry and certification of agreed judgments:

> Absent a claim of fraud or lack of consent, a trial court must approve an

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31. 694 N.E.2d 306, 310 (Ind. Ct. App. 1998). The dispute between these two parties has once again given rise to an appellate issue worthy of comment in this Article. In last year's Article, we discussed the court of appeals' consideration of whether a permissive intervening party in the trial court may maintain an appeal of a judgment when the original parties to the dispute have settled their claims and dismissed the case as between themselves. Wilkins & Blaiklock, *supra* note 2, at 687-89 (discussing that opinion, and that issue). Despite the fact that these two parties have been litigating since February 23, 1993, and it has no doubt been expensive for both parties, they can take solace in the fact that through their appellate machinations they have provided appellate practitioners with insight into some interesting appellate issues. We anxiously await next year's installment.

32. IND. R. APP. P. 3(A).

33. *City of New Haven*, 694 N.E.2d at 310 (citing Appellate Rule 3(A)).

34. *Id.*

35. *Id.*

> agreed judgment. The trial judge has only the ministerial duty of approving the agreed judgment and entering it in the record. However, such a decree does not represent the judgment of the court. It is merely an agreement between the parties, consented to by the court.[36]

There are situations consistent with Appellant Rule 3(A) "in which a trial court may retain jurisdiction and act notwithstanding a pending appeal. Specifically, a trial court retains jurisdiction to perform such ministerial tasks as reassessing costs, correcting the record, or enforcing a judgment."[37] Indeed, a court called upon to make an entry of an agreed judgment "'is not called upon to perform a judicial act. . . . It does not purport to represent the judgment of the court, but merely records the agreement of the parties with respect to the matters in litigation.'"[38]

Therefore, although the trial court, pursuant to Appellate Rule 3(A), lost "general jurisdiction" when the record of the proceedings was filed with the Clerk of the court of appeals, the trial court still retained sufficient "jurisdiction" to enter an agreed judgment, i.e., the simple ministerial duty of ordering the agreement entered in the record.[39]

The court went on to reject the City's argument that the trial court should have reviewed the merits of the agreed judgment.[40] "Unlike the federal courts which appear to have discretion to review substantive provisions of the parties' agreed judgment, this state has repeatedly held that, absent fraud or lack of consent, a trial court *must* approve an agreed judgment."[41] Of Indiana law, the court wrote: "'If an appeal should be allowed from a consent decree, the appellate court would examine the record not to determine error, but to determine whether or not the parties erred in making the stipulation or in giving their consent thereto. Appellate courts do not have such authority.'"[42]

A duty to review the record in that regard is not imposed on a trial court if the person/entity objecting to the agreed judgment was not a party to that agreed judgment. In such cases, a trial court's only duty is to enter an agreed judgment.

D. Indiana Appellate Rule 3(B)

In *Montgomery, Zuckerman, Davis, Inc. v. Chubb Group of Insurance Cos.*,[43] the court of appeals had occasion to review application of Appellate Rule 3(B) which reads in relevant part, "the record of the proceedings must be filed with the clerk of the Supreme Court and Court of Appeals within ninety days from the

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36. *Id.* (citations omitted).
37. *Id.* (citations omitted).
38. *Id.* (quoting State v. Huebner, 104 N.E.2d 385, 387-88 (Ind. 1952)).
39. *See id.*
40. *Id.* at 311.
41. *Id.* (citation omitted) (emphasis added).
42. *Id.* (quoting *Huebner*, 104 N.E.2d at 388).
43. 698 N.E.2d 1251 (Ind. Ct. App. 1998).

date the praecipe is filed."[44] The court's concise review of that rule's application is worthy of inclusion in this survey:

> Filing of the record is a jurisdictional act, and the failure to timely file the record is clear grounds for dismissal of the appeal. Strict compliance with the ninety day time limit of [Appellate Rule] 3(B) is required and failure to do so results in the forfeiture of the right to appeal.[45]

Indiana appellate courts continue to strictly apply Appellate Rule 3(B).[46]

E. Appellate Rule 15

1. Appellate Rule 15(A).—In *WorldCom Network Services, Inc. v. Thompson*,[47] the appellant argued that because the court of appeals' opinion was not published, its chance of having a petition to transfer granted by the Indiana Supreme Court was diminished. In that way, the appellant argued, its due process rights were violated.[48] The court of appeals swiftly rejected that argument, noting that petitions to transfer are granted from both memorandum and published opinions.[49]

2. Jurisdiction to Award Attorneys Fees.—Before the court of appeals in *Montgomery, Zuckerman, Davis, Inc. v. Chubb Group of Insurance Cos.*[50] was the issue of whether it had jurisdiction to enter an award of appellate attorney fees under Appellate Rule 15(G). The court had ruled that it lacked jurisdiction to decide the merits of the appeal because of the appellant's failure to file a record with the clerk of court within ninety days of the timely filed praecipe.[51] Interestingly, the appellee requested an award of appellate attorney fees based on the appellant's conduct in prosecuting the appeal.[52] Appellate Rule 15(G) provides an appellate court with discretionary authority to award damages in favor of an appellee when judgment of the court below is *affirmed*.[53] The court recognized that "at first blush it would appear that [it] lack[ed] the authority to make such an award under the present circumstances under which [it] dismiss[ed]

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44. IND. R. APP. P. 3(B).
45. *Id.* at 1253 (citations omitted).
46. *See, e.g., id.*
47. 698 N.E.2d 1233 (Ind. Ct. App. 1998).
48. *See id.* at 1235.
49. *Id.* at 1242.
50. 698 N.E.2d 1251 (Ind. Ct. App. 1998).
51. *Id.* at 1254.
52. *See id.*
53. *See id.* Indiana Appellate Rule 15(G) states in relevant part:

> If the court on the appeal affirms the judgment, damages may be assessed in favor of the appellee not exceeding ten percent (10%) upon the judgment, in money judgments, and in other cases in the discretion of the court; and the court shall remand such cause for execution.

the appeal for lack of jurisdiction."[54] The court nonetheless held that it had "the inherent authority to make an award of appellate attorney fees under the present circumstances despite the language of App. R. 15(G)."[55] In short, if an appellant is successful in getting the court of appeals to take the time to entertain an appeal, even if the court does not have jurisdiction to rule on the merits of the case, the appellant subjects himself to the risk of being ordered to pay the appellee's attorney fees.

3. Attorney Fees Granted Pursuant to Appellate Rule 15(G).—In *Catellier v. Depco, Inc.*,[56] the court of appeals awarded appellate attorney fees based on the appellant's "procedural bad faith."[57] In doing so, the court set forth a short synopsis of the difference between procedural and substantive bad faith within the context of Appellate Rule 15(G):

> A litigant's bad faith on appeal may be classified as "substantive" or "procedural." Substantive bad faith "implies the conscience doing of a wrong because of dishonest purpose or moral obliquity." Procedural bad faith "is present when a party flagrantly disregards the form and contents requirements of the Rules of Appellate Procedure, omits and misstates relevant facts appearing in the record, and files briefs appearing to have been written in a manner calculated to require the maximum expenditure of time both by the opposing party and the reviewing court." Conduct can be classified as procedural bad faith even if it falls short of being deliberate or by design.[58]

Upon examination of the appellant's brief, the *Catellier* court concluded that the appellant's appeal was "permeated with procedural bad faith."[59] The appellant: (1) "violated Appellate Rule 8.2(A)(4) by submitting an appellate brief that exceeds 30 pages;"[60] (2) wrote a defective statement of the case because it contained argument;[61] (3) violated Appellate Rule 8.3(A)(5) because his statement of the facts contained argument and was not presented in a light most favorable to the judgment;[62] (4) failed to provide pinpoint citation to the cases cited in the brief, in violation of Appellate Rule 8.2(B)(1);[63] (5) failed to

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54. *Id.*

55. *Id. See In re* Matter of Estate of Kroslack, 570 N.E.2d 117, 121 (Ind. Ct. App. 1991) (holding that the court has inherent equitable power to enter an award of attorney fees under the appropriate circumstances); State v. Nessius, 548 N.E.2d 1201, 1205 n.2 (Ind. Ct. App. 1990) (holding that the court of appeals has inherent authority under Appellate Rule 15(N)(6) to grant all appropriate relief on appeal).

56. 696 N.E.2d 75 (Ind. Ct. App. 1998).

57. *Id.* at 79.

58. *Id.* (quoting Watson v. Thibodeau, 559 N.E.2d 1205, 1211 (Ind. Ct. App. 1990)).

59. *Id.*

60. *Id.*

61. *Id.*

62. *Id.*

63. *Id.*

provide cogent arguments in violation of Appellate Rule 8.3(A)(7);[64] and, (6) included unacceptable accusatory statements in the argument.[65] As for the latter, the appellant wrote that "'the trial court seemed determined to enter judgment in favor of [the appellee],' . . . the trial court 'was doing everything it could to fashion a judgment in favor of [the appellee], straining credulity in the process and fabricating legal theories and stretching legal concepts beyond any reason,'" and complained about "'the machinations of the [trial court's] reasoning.'"[66] The court was particularly perturbed with those accusatory statements directed at the trial court, noting that "'the appellate process is not an appropriate forum for these types of blanket accusations, and the accusations are not under any circumstances to be used . . . in place of arguments on the merits.'"[67]

In awarding appellate attorney fees, the court ruled that because of the nature of the procedural bad faith—for which the appellant's attorney was "alone" responsible—it was "appropriate that appellate attorney fees be assessed against [the appellant's] counsel."[68]

4. Appellate Rule 15(N).—In *WorldCom Network Services, Inc. v. Thompson*,[69] the Indiana Court of Appeals had occasion to provide a concise overview of the application of Appellate Rule 15(N).[70]

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64. *Id.*

65. *Id.*

66. *Id.* at 79-80 (quoting Brief of the Appellant, at 17, 31).

67. *Id.* at 80 (quoting Garage Doors of Indianapolis, Inc. v. Morton, 682 N.E.2d 1296, 1305 (Ind. Ct. App. 1997)).

68. *Id.*

69. 698 N.E.2d 1233 (Ind. Ct. App. 1998).

70. Appellate Rule 15(N) states:

> (N) Order or Relief Granted on Appeal. An order or judgment upon appeal may be reversed as to some or all of the parties and in whole or in part. The court, with respect to all or some of the parties or upon all or some of the issues, may order:
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> (1) A new trial;
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> (2) Entry of final judgment;
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> (3) Correction of a judgment subject to correction, alteration, amendment or modification;
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> (4) In the case of claims tried without a jury or with an advisory jury, order the findings or judgment amended or corrected as provided in Rule 52(B);
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> (5) In the case of excessive or inadequate damages, entry of final judgment on the evidence for the amount of the proper damages, a new trial, or a new trial subject to additur or remittitur; or
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> (6) Grant any other appropriate relief, and make relief subject to conditions.
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> The court shall direct final judgment to be entered or shall order the error corrected without a new trial unless such relief is shown to be impracticable or unfair to any of the parties or is otherwise improper; and if a new trial is required it shall be limited only to those parties and issues affected by the error unless such relief is shown to be impracticable or unfair. A judgment may be affirmed on conditions. A verdict, finding, judgment, order or decision shall be reversed upon appeal as not supported by or as

> Indiana Appellate Rule 15(N) provides that this court may order the trial court to amend or correct its findings that a judgment may be affirmed on conditions. Although we affirmed the trial court's judgment, we were not obliged to adopt or approve its findings. A trial court finding that is not supported by or is contrary to the evidence may be reversed on appeal if clearly erroneous. The rules further allow us to order findings amended or corrected and to grant any other appropriate relief.[71]

II. Common Law Appellate Jurisprudence

A. Law of the Case

During the survey period there were several cases that considered the "law of the case" doctrine.[72] That doctrine "'mandates that an appellate court's determination of a legal issue binds both the trial court and the court on appeal in any subsequent appeal involving the same case and relevantly similar facts.'"[73] The purpose of the doctrine is to avoid the relitigation of issues already resolved by an appellate court.[74] To that end, relitigation is barred for all issues decided "directly or by implication in a prior decision."[75]

The extent to which an issue decided in a prior ruling is binding was examined in *Stepp v. Duffy*.[76] In *Stepp*, the court of appeals affirmed an award of trial attorney fees and remanded the case to the trial court for consideration of the underlying damage issue related to the merits of the case.[77] On remand, the trial court complied with the court of appeals directive on the damage issue, and reiterated its award of trial attorney fees. In addition, the trial court considered the appellee's post-appeal petition for post-judgment attorney fees, and awarded those fees to the appellee.[78] In the second appeal, the appellant argued that upon remand the trial court only had jurisdiction to decide the issue of damages, and that the "law of the case" doctrine precluded the trial court from awarding post-judgment attorney fees.[79] In summarizing the applicable law, the court in *Stepp*

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contrary to the evidence only when clearly erroneous, and due regard shall be given to the opportunity of the finder of fact to judge the credibility of witnesses.

71. *WorldCom Network Services*, 698 N.E.2d at 1237 (citations omitted).

72. *See* United of Omaha v. Hieber, 698 N.E.2d 869 (Ind. Ct. App. 1998); Hoovler v. State, 689 N.E.2d 738 (Ind. Ct. App. 1997); Stepp v. Duffy, 686 N.E.2d 148 (Ind. Ct. App. 1997).

73. *Hoovler*, 689 N.E.2d at 742 (quoting St. Margaret Mercy Healthcare Ctrs., Inc. v. Ho, 663 N.E.2d 1220, 1223 (Ind. Ct. App. 1996)).

74. *See id.*

75. *Id.* (quoting Certain N.E. Annexation Area Landowners v. City of Fort Wayne, 662 N.E.2d 548, 549 (Ind. Ct. App. 1993)).

76. 686 N.E.2d 148 (Ind. Ct. App. 1997).

77. *Id.* at 150.

78. *See id.* at 151.

79. *See id.* at 152.

wrote:

> [A] trial court, once it has been divested of jurisdiction of a case, does not have jurisdiction to void its prior judgment. . . . [W]hether the trial court upon remand has jurisdiction to make additional factual inquiries or to hear new issues depends upon what issues are decided upon appeal and what issues are expressly or impliedly reserved upon remand. . . . [T]he general rule of "law of the case" is a discretionary rule of practice which, unlike the doctrine of *res judicata*, need not be uniformly and rigidly applied. The limitation upon a trial court's jurisdiction after a remand is based upon the expectation that the trial court will do what it was requested to do by the appellate court. An appellate court retains jurisdiction to see that its instructions are carried out.[80]

Accordingly, the appellate court determined that the trial court was not attempting to impermissibly void its prior judgment by ruling on the appellee's motion for post-judgment attorney fees, nor was consideration of that petition controlled by the "law of the case" doctrine.[81]

In *United of Omaha v. Hieber*,[82] the court of appeals decided an ERISA issue. The case then went to the trial court on remand, and came back up to the court of appeals a second time. Between the time of the first and second court of appeals' opinions, the Seventh Circuit Court of Appeals issued opinions bearing on the ERISA question decided in the first court of appeals' opinion.[83] In the second opinion, the court of appeals ruled that "[t]he law of the case doctrine allowed [it] to reconsider its [first] holding in light of the intervening Seventh Circuit decisions."[84]

B. New Argument on Appeal

In *Northern Indiana Commuter Transportation District v. Chicago Southshore*,[85] the supreme court considered the issue of whether a party can raise new constitutional arguments for the first time in a petition for rehearing, when the need to raise those arguments did not arise until after, and because of, the court of appeals' opinion. In short,[86] in *Chicago Southshore* the appellant did not raise Full Faith and Credit Clause arguments before the court of appeals until its petition for rehearing, even though it technically could have done so. The appellant did not do so because it did not perceive the need to do so. It was only upon issuance of the court of appeals' opinion that the real need for a

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80. *Id.* at 152 (citations and quotations omitted).
81. *Id.*
82. 698 N.E.2d 869 (Ind. Ct. App. 1998).
83. *See id.* at 874.
84. *Id.* at 874 n.4.
85. 685 N.E.2d 680 (Ind. 1997).
86. This decision has a complex procedural background. For details in addition to those provided, the reader is directed to the full opinion.

constitutional argument arose.[87]

The appellee argued that consistent with established Indiana appellate jurisprudence, "new claims or issues, including constitutional arguments . . . cannot be presented for the first time in a petition for rehearing."[88] The appellant responded by arguing that "it did not raise the issue until rehearing because under the procedural posture of [the] appeal it would have been premature to do so earlier."[89] The supreme court ruled in favor of the appellant, first noting that "[t]here are sound reasons for requiring a party to present all known arguments or claims to an appellate court before its decision is rendered. Rehearing opinions exhaust precious judicial resources that could be expended elsewhere."[90] However, a different standard must be applied when a litigant is claiming the deprivation of a federal constitutional right "due to a surprising and unforeseeable result on appeal."[91] To invoke this rule, the appellant must be able to convince the reviewing court that the ruling "could not have been anticipated and prevented [the appellant] from feeling the need to raise its federal constitutional issue at an earlier time."[92] In reaching its ruling, the supreme court stated:

> Where a state court acts in an unanticipated way to deprive a party of the opportunity to make an argument or present a valid defense based on the Federal Constitution, the issue is not waived for purposes of review by the Supreme Court of the United States. As Justice Cardozo succinctly summarized . . . "The settled doctrine is that when a constitutional privilege or immunity has been denied for the first time by a ruling made upon appeal, a litigant thus surprised may challenge the unexpected ruling by a motion for rehearing, and the challenge will be timely." This standard is met where the trial court disposed of the case on the basis of subject-matter jurisdiction and the appellate court not only reverses on that issue, but resolves the merits of the dispute without briefing or argument by the parties. Accordingly, this [c]ourt should entertain the issue as a matter of Indiana appellate procedure. Finding waiver here could needlessly present an incorrect decision on a matter of federal constitutional law to the Supreme Court of the United States.[93]

It will be interesting to see whether the *Chicago Southshore* decision is limited to those cases in which the litigant will be precluded from advancing a constitutional argument or whether the decision will serve as a springboard for expanded use of the decision in non-constitutional cases. Either way, the result

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87. *See Chicago Southshore*, 685 N.E.2d at 685-86.

88. *Id.* at 686 (citing City of Indianapolis v. Wynn, 159 N.E.2d 572 (Ind. 1959)).

89. *Id.*

90. *Id.* at 687.

91. *Id.*

92. *Id.*

93. *Id.* (quoting Herndon v. Georgia, 295 U.S. 441, 447 (1935) (Cardozo, J., dissenting), other citation omitted).

reached in *Chicago Southshore* preserves a fundamental principle of our judicial systems, namely: A party deserves his day in court to present his best argument.

C. *Striking of Scandalous Brief*

In *WorldCom Network Services, Inc. v. Thompson*,[94] the court of appeals took the unusual step of striking portions of an appellate brief. In *WorldCom*, the appellants, in their brief in support of rehearing, included what the court of appeals perceived to be an attack on the court of appeals itself.[95] The court distinguished the attack from appropriate advocacy, in which an "advocate can present his cause, protect the record for subsequent review and preserve professional integrity by patient firmness no less effectively than by belligerence or theatrics."[96] To that end, "[j]udges and attorneys are engaged in a common enterprise and have a joint obligation and privilege to improve the legal order."[97] The court of appeals determined that "[t]he incivility manifested in the [appellants'] petition and brief corrodes the judicial system."[98] The court noted that portions of the appellants' brief did present cogent argument; however, "the strident and offensive tenor of the remaining portions interferes with this court's due deliberation on the merits of those issues which the [appellants] ask us to consider on rehearing. Their overheated rhetoric is unpersuasive and ill-advised."[99] The appellants' "righteous indignation [was] no substitute for a well-

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94. 698 N.E.2d 1233 (Ind. Ct. App. 1998).

95. *Id.* at 1236.

96. *Id.* at 1237.

97. *Id.*

98. *Id.* The extent to which the appellants "corroded" the judicial system is described by the court as follows:

> While the Thompsons profess to hold this court in "high esteem," significant parts of their petition and brief are condescending and permeated with sarcasm and disrespect. By way of illustration, they allege that our decision, if not corrected, "can only lead to ridicule, if not contempt, for this Court by the Thompsons and their many friends and neighbors," and that "[t]oo many citizens are already cynical, if not contemptuous, of the judiciary." They assert that our decision contains "glaringly incorrect statements of supposed fact," which are "obviously wrong." They imply that the court lacks experience in real estate matters.
>
> The Thompsons also accused the court of writing "with pens filled with the staining ink of innuendo," allege that portions of our decision give "the appearance of bias, prejudice and impropriety" and argue that "the decision will remain as a blemish on the record" of the court if those portions are not retracted. They assert that if this court were to disagree with a certain finding "it would be ridiculous," and then question the court's good faith and ethics. They demand an "apology" from the court. At one point, in rhetorical high gear, the Thompsons warn the court against reaching a particular conclusion and declare that such a ruling would be "blatantly erroneous."

Id. at 1236.

99. *Id.*

reasoned argument."[100]

Thus, relying on its general authority to strike scandalous or impertinent material, the court of appeals struck "the inappropriate portions of the [appellants'] petition and brief."[101] Even though the "offensive material [was] so interwoven with legitimate argument that the court considered striking the entire submission," the court acted mercifully and did not do so because it did not believe the appellants "should be denied consideration of their petition due to the excessive zeal of their attorneys."[102] Only the offensive portions were stricken, and the court admonished counsel that the use of impertinent material "disserves the client's interest and demeans the legal profession."[103]

WorldCom sets forth in no uncertain terms that directing frustration with an opinion believed to be wrong at the court itself, rather than to the substance of the opinion, is ill-advised and will not be looked upon lightly by Indiana's appellate courts.

D. Advisory Opinions

The court in *WorldCom* also held that it did not violate the constitutional rights of the parties for a court to issue an advisory opinion when, after remanding a matter in which an appeal had been taken from the denial of injunctive relief, it addressed other issues that were likely to recur on remand.[104] In so ruling, the court noted that it addressed only those issues that had been briefed by the parties before the trial court and on appeal.[105] Given the procedural posture of the case, the court felt it was in the interest of judicial economy to correct errors made by the trial court that were likely to recur on remand, citing Appellate Rule 15(N) for its authority to do so.[106]

E. Constitutional Right to Transfer

In *WorldCom* the court reaffirmed the proposition that the "Indiana [C]onstitution provides the right to one appeal, which is to the Court of Appeals."[107] Thus, "[t]here is no constitutional right of transfer to [the Indiana S]upreme [C]ourt."[108]

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100. *Id.* at 1236-37.
101. *Id.* at 1237.
102. *Id.*
103. *Id.*
104. *Id.*
105. *Id.*
106. *Id.*
107. *Id.* at 1242 (citing IND. CONST. art. VII, § 6).
108. *Id.*

III. Indiana Trial Rules and Appellate Practice

In *Mitchell v. Mitchell*,[109] the supreme court made an extremely important ruling with respect to the standard of review applicable to cases in which Indiana Trial Rule 52(A) is utilized.[110] Until *Mitchell*, appellate courts in Indiana followed "the doctrine that where special findings are requested and entered under Trial Rule 52(A) the appellate court is not to affirm the trial court based on any legal theory, but rather is limited to the theory of law adopted by the trial court."[111] The supreme court noted that "the rationale for this doctrine has rarely been explained and its genesis is not entirely clear."[112]

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109. 695 N.E.2d 920 (Ind. 1998).

110. Indiana Trial Rule 52(A) states:

> (A) Effect. In the case of issues tried upon the facts without a jury or with an advisory jury, the court shall determine the facts and judgment shall be entered thereon pursuant to Rule 58. Upon its own motion, or the written request of any party filed with the court prior to the admission of evidence, the court in all actions tried upon the facts without a jury or with an advisory jury (except as provided in Rule 39[D]) shall find the facts specially and state its conclusions thereon. The court shall make special findings of fact without request
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> (1) in granting or refusing preliminary injunctions;
>
> (2) in any review of actions by an administrative agency; and
>
> (3) in any other case provided by these rules or by statute.
>
> On appeal of claims tried by the court without a jury or with an advisory jury, at law or in equity, the court on appeal shall not set aside the findings or judgment unless clearly erroneous, and due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses. The findings of a master, and answers to questions or interrogatories submitted to the jury shall be considered as findings of the court to the extent that the court adopts them. If an opinion or memorandum of decision is filed, it will be sufficient if the findings of fact and conclusions appear therein. Findings of fact are unnecessary on decisions of motions under Rule 12 or 56 or any other motion except as provided in Rule 41(B) (dismissal) and 59(J) (motion to correct errors).

111. *Mitchell*, 695 N.E.2d at 922. "The [c]ourt of [a]ppeals understandably invoked this rule because it (or similar or variant rules) has been cited repeatedly by the [c]ourt of [a]ppeals, particularly in recent years." *Id.* (citing Castillo-Cullather v. Pollack, 685 N.E.2d 478, 481 (Ind. Ct. App. 1997), *trans. denied*; Showalter, Inc. v. Smith, 629 N.E.2d 272, 274 (Ind. Ct. App. 1994)).

112. *Id.* The supreme court stated:

> The decisional law, while on balance favoring the rule by rote citation to early authorities, is not uniform. One antecedent appears to be *Shrum v. Dalton*, 442 N.E.2d 366, 372 (Ind.Ct.App. 1982), a case involving sua sponte findings that declared without citation that "where special findings are made, this court may not affirm the judgment of the trial court on any ground which the *evidence* supports." This is a different proposition from whether an affirmance may rest on the facts as found but under a different legal theory. However, the former seems to have morphed into the latter in recent years. The *Shrum* rule was soon restated in *Orkin Exterminating Co. v. Walters*, 466 N.E.2d 55, 56 (Ind. Ct. App. 1984), a case eventually cited for the rule relied on by

The court was presented with an interesting application of that standard of review in *Mitchell*. In its Trial Rule 52(A) findings, the trial court adopted, and rested its ruling upon, an incorrect legal theory.[113] However, there was a legal theory other than that relied upon by the trial court upon which the court of appeals could have affirmed the trial court's decision, but for the traditional standard of review in cases involving Trial Rule 52(A). The supreme court, applying a common sense approach, found no reason why "a correct rule of law applied to facts found by the trial court may not result in affirmance of the judgment even if the trial court reached the same result through a different legal theory, particularly where the dispositive alternative theory was briefed by both parties on appeal."[114]

The supreme court held:

> Trial Rule 52(A) is a method for formalizing the ruling of the trial court, providing more specific information for the parties, and establishing a particularized statement for examination on appeal. These purposes are not inconsistent with affirming to reach the right result on appeal under the law applied to the facts as found. Accordingly, we hold that where a trial court has made special findings pursuant to a party's request under

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> the [c]ourt of [a]ppeals here. *See* Vanderburgh County Bd. of Comm'rs v. Rittenhouse, 575 N.E.2d 663, 665-66 (Ind. Ct. App. 1991) (citing inter alia *Orkin Exterminating Co.*[, 466 N.E.2d at 55]). Other early decisions setting forth the doctrine cited pre-Trial Rules cases, *see* National Fleet Supply, Inc. v. Fairchild, 450 N.E.2d 1015, 1019 (Ind. Ct. App. 1983) (citing Miller v. Ortman, [] 136 N.E.2d 17 (1956)), or decisions dealing with different issues altogether. *See* City of Hammond v. Conley, 498 N.E.2d 48, 52 (Ind. Ct. App. 1986) (citing *Orkin Exterminating Co.*[, 466 N.E.2d at 55;] *In re* Estate of Fanning, [] 333 N.E.2d 80 (1975) [(reject[ing] a general judgment standard of review under the facts presented but did not clearly involve review of special findings under Trial Rule 52)]), *overruled on other grounds by* Osler Institute, Inc. v. Inglert, 569 N.E.2d 636, 637 (Ind. 1991) (per curiam)[)]. In contrast, at least two decisions contain some language suggesting that affirmance on any legal theory supported by the trial court's findings is permissible. Lawyers Title Ins. Corp. v. Pokraka, 595 N.E.2d 244, 249 (Ind. 1992) (unclear whether findings were requested or entered sua sponte); Data Processing Services, Inc. v. L.H. Smith Oil Corp., 493 N.E.2d 1272, 1274-75 (Ind. Ct. App. 1986). Finally, one case involving requested special findings, without citation to authority or any apparent consideration of the *Shrum* line of decisions, applied a general judgment standard of review to the same issue presented here—an award of attorney's fees. United Farm Bureau Mut. Ins. Co. v. Ira, 577 N.E.2d 588, 597-98 (Ind. Ct. App. 1991).

Id. at 922 n.3 (citation format corrected).

113. *See id.* at 923.

114. *Id.* "Because no additional fact finding is needed, the appellate court is equally well positioned to address application of the alternative theory in the first instance. Indeed, it is routine in other context for appellate courts to affirm judgments on theories other than those adopted by the trial court." *Id.*

> Trial Rule 52(A), the reviewing court may affirm the judgment on any legal theory supported by the findings. Whether it is prudent to do so may turn on the extent to which the issue is briefed on appeal. In this case, both parties expressed their views on the correct rule of law in the [c]ourt of [a]ppeals. Under these circumstances, there is no surprise and no risk of the appellate court's introducing an unvetted legal theory. In addition, before affirming on a legal theory supported by the findings but not espoused by the trial court, the appellate court should be confident that its affirmance is consistent with all of the trial court's findings of fact and the inferences reasonably drawn from the findings.[115]

This ruling gives appellants wider latitude in framing arguments before Indiana appellate courts. Trial Rule 52(A) no longer has the limiting effect it once did. Accordingly, *Mitchell* must now be taken into consideration when making the decision at the trial court level about whether to request special findings under Trial Rule 52(A).

CONCLUSION

During the survey period, several opinions of importance were issued with respect to appellate practice. As always, appellate practitioners are urged to keep an eye on how Indiana's appellate courts interpret the Appellate Rules during the year. It is evident from our review of the cases during this survey period, and those of last year's survey, that the Indiana Supreme Court continues to issue opinions directed at making appellate practice consistent and predictable. Finally, Indiana's courts of appeal appear to be increasingly less tolerant of overzealous advocacy.

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115. *Id.* at 923-24 (citation omitted).

SURVEY OF RECENT DEVELOPMENTS IN INSURANCE LAW

RICHARD K. SHOULTZ*

INTRODUCTION

During each of the past few survey years, at least one decision on insurance law has deserved special attention. However, during the most recent survey period,[1] the Indiana appellate courts failed to address any insurance decisions that will have a monumental impact on all practitioners. Nevertheless, a number of significant cases were decided, which cover many areas including automobile, homeowners, commercial liability, health, and medical insurance policies. This Article discusses these decisions and their effect on the practice of insurance law.

I. AUTOMOBILE INSURANCE CASES

A. Permissive Use

One of the more interesting cases from the survey period involved the question of a truck driver's permissive use of an automobile after consuming alcohol. In *Warner Trucking, Inc. v. Carolina Casualty Insurance Co.*,[2] the owner of a trucking company expressly forbid all truck drivers from consuming alcohol on the days they drove company trucks.[3] One of the company's drivers consumed alcohol at a fellow employee's party on the evening before he was to begin an early morning journey. The driver left the party and was dropped off at his truck to sleep before leaving on the trip. During the evening, the truck driver drove away and collided with another vehicle, injuring the occupants.[4]

The injured victims filed a lawsuit against the driver and his employer.[5] The trucking company's liability insurance carrier filed a separate declaratory judgment lawsuit to disclaim coverage for the employee. The two cases were consolidated for resolution. For both the personal injury lawsuit and the declaratory judgment action, the supreme court addressed issues concerning permissive use of the truck by the driver.[6]

Warner Trucking filed a Motion for Summary Judgment in the victims' personal injury lawsuit, contending that the driver's action of driving the vehicle after consuming alcohol violated the company's rule prohibiting such conduct. Thus, the trucking company argued that it could not be responsible because the driver was not acting within the scope of his employment at the time of the

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* Partner, Lewis & Wagner. B.A., 1987, Hanover College; J.D., 1990, Indiana University of Law—Indianapolis.

1. The survey period for this Article is approximately September 1, 1997 to August 1, 1998.
2. 686 N.E.2d 102 (Ind. 1997).
3. *See id.* at 104-05.
4. *See id.* at 105.
5. *See id.* at 104.
6. *Id.* at 105, 107.

accident.[7]

The supreme court disagreed with the trucking company's argument as a matter of law.[8] While the supreme court acknowledged that the driver's behavior in violating the rule is a consideration in determining "scope of employment," it is not solely determinative.[9] The key to determining scope of employment is whether the employee's action benefits or serves his employer.[10] If the employee's action, even if in violation of the employer's rules, provides any benefit to the employer, then a factual issue remains as to whether the employee was acting within the scope of employment.[11]

The employer's liability insurance company also filed a Motion for Summary Judgment on the question of insurance coverage for the driver.[12] Specifically, the insurer argued that in order for the driver to qualify as an "insured," he must be operating the vehicle with permission.[13] Because the company expressly forbid operating a truck after consuming alcohol, the driver did not have permission and was not an insured.[14]

The supreme court agreed with the insurer's argument.[15] Unlike the "scope of employment" issue, the court found the driver's violation of the company's prohibition to be determinative of his permission:

> When the owner of a vehicle places express restrictions on its use by others, the focus is not on whether the operator deviated from the contemplated use; the determinative question is whether *the operator's use of the vehicle was restricted in the first instance*. In a coverage dispute, permissive use cannot be implied when an express restriction on the scope of permission prohibits the use at issue.[16]

Thus, the driver did not have permission and did not qualify for insurance coverage under his employer's policy.[17]

B. Resident of Household

With many forms of convenient transportation available in today's society,

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7. *See id.* at 105.
8. *Id.*
9. *Id.*
10. *See id.*
11. *See id.* at 105-06; *see also* Eagle Motor Lines, Inc. v. Galloway, 426 N.E.2d 1322, 1325-26 (Ind. Ct. App. 1981).
12. *See Warner Trucking*, 686 N.E.2d at 106.
13. *See id.* at 106. The language of the policy defined an "insured," in relevant part, as "[a]nyone . . . while using with your permission a covered truck you own, hire or borrow." *Id.*
14. *See id.*
15. *Id.* at 107.
16. *Id.* (quoting State Farm Mut. Auto. Ins. v. Gonterman, 637 N.E.2d 811, 814 (Ind. Ct. App. 1994) (emphasis in original)).
17. *Id.*

people often become transient in their living arrangements. Thus, a common question focuses on where a person resides for purposes of determining insurance coverage.[18] This question is addressed in *Chance v. State Auto Insurance Cos.*[19]

A student's family moved from Marion to Fort Wayne. The student had difficulties with the Fort Wayne school, so his parents sent him to stay with his brother and attend the local school in Marion.[20] In order for the student to attend the Marion school without paying tuition, the parents completed an agreement that stated, in part, that the main reason for the student's move was not so he could attend the Marion school.[21]

The student was killed while riding in a car with an uninsured driver. The student's estate received uninsured motorist benefits from his brother's insurance policy, but also sought to acquire uninsured motorist coverage under his parents' policy.[22] In order for coverage to be available under the parents' policy, the student needed to be "a resident of [the parents'] household."[23]

The court of appeals affirmed the trial court's grant of summary judgment in favor of the insurer, by concluding that the student was not a "resident" of the parents' household at the time of his death.[24] While the court acknowledged that the interpretation of "resident" for an insurance policy is to be given a broad meaning, the court determined that the evidence prevented a finding that the student had more than one residence.[25] The parents were estopped from arguing that the student had two residences so that he could attend school in Marion, when they had executed an agreement that contradicted this argument.[26]

Unlike decisions by other courts,[27] this ruling holds that the student did not have two residences. A dissenting opinion argued that the student had two residences, because Indiana recognizes that a student remains a part of his parents' household while away for educational purposes.[28] However, the dissent ignores the parents' execution of an agreement which expressly stated the student was not living with his brother to attend school. This fact distinguishes the

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18. In last year's survey period, the decision in *Erie Insurance Exchange v. Stephenson*, 674 N.E.2d 607 (Ind. Ct. App. 1996), addressed this same issue. *See* Richard K. Shoultz, 31 IND. L. REV. 695, 701 (1998).

19. 684 N.E.2d 569 (Ind. Ct. App. 1997), *trans. denied*, 698 N.E.2d 1187 (Ind. 1998).

20. *See id.* at 570.

21. The agreement specifically provided that "[t]he student was placed with the custodian by the student's parent(s). The custodian is supporting and caring for the student. *The student was not placed with the custodian for the primary purpose of attending school in the school corporation of the custodian's residence.* *Id.* at 570 n.1 (emphasis added).

22. *See id.* at 570.

23. *Id.*

24. *Id.* at 571.

25. *Id.*

26. *See id.*

27. *See* Shoultz, *supra* note 18, at 701.

28. *Chance*, 684 N.E.2d at 572 (Robertson, J., dissenting). The dissenting judge cited a number of cases which support this rationale. *Id.* at 571-72.

Chance case from other decisions which concluded that an insured may have more than one residence for purposes of identifying insurance coverage.

C. *Interpretation of Auto Repair Business Exclusion*

Personal automobile insurance policies are generally intended to provide liability coverage for the named insured and persons he permits to drive his vehicle. However, one issue is how far that coverage should extend when the insured entrusts his automobile to a repair shop. The question is addressed in *Barga v. Indiana Farmers Mutual Insurance Group, Inc.*[29]

The insured took his vehicle to a dealership for repair.[30] The dealership's mechanic could not discover the problem and began to drive the truck on personal endeavors in hopes of identifying what was wrong with the truck.[31] One evening, while the mechanic was driving the vehicle for personal use, he was involved in a serious automobile accident. The injured victim filed a lawsuit against the mechanic and the dealership to recover for personal injuries. The trial court entered judgment in favor of the victim, which exhausted the insurance coverage available to the dealership and mechanic.[32] The injured victim then sought to acquire additional damages from the vehicle owner's policy.[33] The insurance company for the owner sought to deny coverage based upon a provision which excluded coverage for "'bodily injury and property damage arising out of auto business operations.'"[34]

In a split decision, the appellate court reversed the granting of summary judgment for the insurance company.[35] The court first found that the victim was not judicially estopped from arguing that her injuries did not "arise out of the business operations" at the time of the accident.[36] The victim initially argued that the mechanic was "in the course of his employment" in order to establish liability against the dealership and to obtain the dealership's insurance coverage.[37] However, the victim contended that her present position, that her injuries did not "arise out of business operations," was not inconsistent with her initial position because the phrases "in the course of" and "arising out of" are not synonymous.[38]

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29. 687 N.E.2d 575 (Ind. Ct. App. 1997), *trans. denied*, 698 N.E.2d 1193 (Ind. 1998).

30. *See id.* at 576.

31. *See id.* There is no mention by the court as to whether the insured consented to the mechanic driving the vehicle for personal use.

32. *See id.*

33. *See id.*

34. The exact language of the exclusion stated: "Bodily injury or property damage arising out of auto business operations. But, coverage does apply to the ownership, maintenance, or use of your insured car in auto business operations by you, a relative, or anyone associated with or employed by you or a relative in the business." *Id.* at 577.

35. *Id.* at 579.

36. *Id.* at 577.

37. *See id.*

38. *See id.*

The court agreed with the victim.[39]

After interpreting the policy, two judges voted to reverse the summary judgment because factual issues existed preventing summary judgment.[40] The mechanic's operation of the vehicle involved both personal and business use.[41] Consequently, whether the accident arose out of auto business operations must be addressed by the trier of fact.[42]

This case amply demonstrates how resolution of an insurance coverage question can be fact sensitive. The mechanic would not have had the vehicle but for his need to complete a repair which is part of a business operation. However, at the time of the accident, a factual uncertainty remained as to whether the mechanic's venture was related to business because he was using the vehicle for personal use.

D. Bad Faith on Uninsured Motorist Claim

With Indiana's judicial recognition that an insured may pursue a claim for bad faith by his insurance company in the handling of a claim,[43] a practitioner representing an insured may allege that an insurance company has engaged in bad faith, without any rational basis upon which to base the claim. The Indiana Court of Appeals addressed such a situation, where the insurance company clearly did not act in bad faith in addressing a claim, in *Becker v. American Family Insurance Group*.[44]

The insured sustained personal injuries in an automobile accident with an uninsured motorist.[45] The insured submitted an uninsured motorist claim to his own carrier, which was initially denied because the insurance company believed the policy had been canceled. Upon realizing that the cancellation was erroneous, the insurance company reinstated the policy and investigated the accident.[46]

After the investigation was completed, the insurance company again denied the claim. The company believed the insured was greater than fifty percent at fault, which prohibited recovery under the policy.[47] The insured filed suit against the insurer seeking uninsured motorist coverage and alleging that the insurer acted in bad faith by denying the claim.

The trial court bifurcated the uninsured motorist claim from the claim for bad faith.[48] A jury heard the evidence and returned a verdict for the insured, but

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39. *Id.*
40. *Id.* at 579 (Sullivan, J., concurring & Gerrard, J., dissenting).
41. *See id.*
42. *See id.*
43. *See* Erie Ins. Co. v. Hickman, 622 N.E.2d 515, 519 (Ind. 1993).
44. 697 N.E.2d 106 (Ind. Ct. App. 1998).
45. *See id.* at 107.
46. *See id.*
47. *See id.*
48. *See id.*

assessed the insured's comparative fault at forty-five percent.[49] As a result, the insurer filed a Motion for Summary Judgment arguing that, as a matter of law, the insurance company did not act in bad faith.[50] The trial court granted summary judgment for the insurance company, which was later affirmed on appeal.[51]

The appellate court reiterated the well-established principal that an insurance company's right to dispute a claim is not tantamount to bad faith:

> [A] good faith dispute about the amount of a valid claim or about whether the insured has a valid claim at all will not supply the grounds for a recovery in tort for the breach of the obligation to exercise good faith. This is so even if it is ultimately determined that the insured breached its contract. That insurance companies may, in good faith, dispute claims, has long been the rule in Indiana.[52]

The jury's ultimate determination that the insured was forty-five percent at fault clearly demonstrated the difficulty of determining the insured's fault.[53] Because the jury's verdict was close to the insurance company's assessment of comparative fault, the appellate court found, as a matter of law, that the insurer did not act in bad faith.[54]

This case emphasizes that insurance companies *do not* engage in bad faith, merely by disagreeing with the insured over the value or liability assessment of a claim. Insurance companies possess a "right to disagree," without fear that they have engaged in bad faith. Practitioners who represent insureds should be mindful of this decision and refrain from making unsubstantiated allegations of bad faith against an insurance company. Instead, a claim for bad faith should be used only when insurance companies engage in more egregious behavior than disputing the value of a claim.

E. Assignability of Bad Faith Action

In a case of first impression, the Indiana Court of Appeals determined that a claim for punitive damages was assignable in *Allstate Insurance Company v. Axsom*.[55] The plaintiff sustained serious injuries in an automobile accident.[56] The defendant possessed limits of $50,000 from his insurer. At trial, the plaintiff offered to settle the case for policy limits but the insurance company, acting on behalf of the defendant, rejected the offer. The jury returned with a verdict in favor of the plaintiff for $80,500, which was in excess of the available insurance

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49. *See id.*
50. *See id.*
51. *Id.* at 108.
52. *Id.* (quoting Erie Ins. Co. v. Hickman, 622 N.E.2d 515, 520 (Ind. 1993)).
53. *Id.*
54. *Id.*
55. 696 N.E.2d 482 (Ind. Ct. App. 1998).
56. *See id.* at 484.

coverage.[57]

The defendant assigned to the plaintiff any rights which the defendant possessed against the insurance company.[58] The plaintiff asserted that the insurance company acted in bad faith for failing to settle within policy limits and sought punitive damages and attorney fees. After the trial court granted summary judgment to the insurance company on the plaintiff's attempt to recover punitive damages, the plaintiff appealed.[59]

The Indiana Court of Appeals focused on the ability of a party to assign to another a claim for punitive damages. While the court recognized Indiana's rule against assigning causes of actions for personal injuries,[60] the court determined that a claim for punitive damages could be assigned because it was a claim for property damage rather than for personal injury.[61] The court also relied on an Arizona Court of Appeals decision, which refused to permit recovery under an assignment for personal injury damages such as "pain and suffering, embarrassment, mental anguish and humiliation."[62] Instead, the damages were limited to the pecuniary loss of the insured—the excess judgment—as well as punitive damages.[63]

In deciding that a claim for punitive damages is assignable, the court supported its decision by noting that permitting this assignment would serve the purpose of "forc[ing] insurance companies to deal in good faith with their insureds as opposed to unreasonably exposing them to personal liability if a jury were to return a verdict in excess of policy limits."[64] Thus, despite the court's statement in a footnote that it was not addressing whether a claim for an insurer's bad faith refusal to settle is assignable, the court seems to have determined that the tort of bad faith is assignable based on the purpose behind awarding punitive damages.[65] While it remains unclear whether an insured may assign a claim for the tort of bad faith, it would appear the court is leaning toward permitting such an assignment.

F. Misrepresentation in Application for Insurance

Although a number of cases address the effect of material misrepresentations

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57. *See id.*

58. *See id.*

59. *See id.*

60. *Id.* at 485. *See* Picadilly, Inc. v. Raikos, 582 N.E.2d 338, 340 (Ind. 1991).

61. *Axsom*, 696 N.E.2d at 485.

62. *Id.* (quoting Clearwater v. State Farm Mut. Auto. Ins. Co., 780 P.2d 423, 427 (Ariz. Ct. App. 1989), *vacated in part by* 792 P.2d 719 (Ariz. 1990)).

63. *Id.*

64. *Id.* at 486.

65. In its footnote, the court observed that "[n]either [the plaintiff] nor [the insurer] discusses in their briefs whether a tort action for an insurer's bad faith failure to settle is assignable. We reserve for another day a detailed discussion of this issue. For the sake of argument we assume its assignability." *Id.* at 484 n.1.

by an insured in the acquisition of insurance, the Indiana Supreme Court, in a well-written opinion, discussed the issue in *Colonial Penn Insurance Co. v. Guzorek*.[66] A wife filled out a policy application, but did not disclose that her husband's driver's license had been suspended or that her husband had continued to drive.[67] While he was driving his wife's vehicle, the husband was involved in an automobile accident.

Before addressing the misrepresentation issue, the court discussed whether the vehicle driven by the husband was covered under the policy.[68] The wife had acquired the new vehicle twenty-nine days before the accident.[69] The couple argued that coverage existed because the vehicle was either an "additional"[70] or "replacement"[71] vehicle as defined under the policy.

The court determined the vehicle did not fall within either of these provisions.[72] Because the wife did not notify the insurer of the vehicle's acquisition within the first thirty days after purchase, the wife did not follow the policy requirements that trigger coverage.[73] The court refused to find that coverage automatically existed for the thirty-day period during which the insured failed to notify the insurer that she had purchased a car.[74]

Likewise, the court also refused to find that the new vehicle qualified as a "replacement" automobile.[75] Because the wife never actually disposed of another vehicle, the court found that the new vehicle did not "replace" another car and denied coverage.[76]

Next, the court focused upon the misrepresentation in the policy application. The parties did not dispute that the wife made a misrepresentation by not including her husband's driving suspension as well as his continued driving.[77]

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66. 690 N.E.2d 664 (Ind. 1997).

67. *See id.* at 666.

68. *Id.* at 668.

69. *See id.*

70. The "additional" car provision stated in relevant part:

> If We insure all your private passenger autos . . . at the time You get the additional auto or truck, We'll automatically consider it to be listed on your Declarations Page. It will have the same coverages as your other autos. For the coverages to apply, however, You must notify us within 30 days after getting the vehicle . . . and pay an additional premium.

Id. (emphasis omitted).

71. The policy defined "replacement" car as: "You may replace a listed auto with another private passenger auto, during the policy period. If You do, We'll automatically consider the replacement to be listed. The coverages You bought for your former auto will apply to the replacement." *Id.* at 670. (emphasis omitted).

72. *Id.* at 671.

73. *See id.* at 669.

74. *Id.* at 670.

75. *Id.* at 670-71.

76. *Id.*

77. *See id.* at 673.

Likewise, because the husband was automatically covered under the wife's policy, the misrepresentation was "material" because the insurer's underwriting guidelines prohibited offering coverage to applicants in this situation.[78]

The court focused on whether the insurer could rescind the policy based upon a material misrepresentation of the insured.[79] The court first concluded that the public policy concerns under Indiana's Financial Responsibility Act,[80] permitted rescission for material misrepresentations.[81] The court also determined that the insurance company could rescind the policy because of the material misrepresentations made by the wife in applying for insurance.[82] Either as a spouse or because of his driving record, the husband's absence from the application was material such that the insurance company would not have written the policy had it known of his presence or driving record.[83]

II. HOMEOWNERS AND COMMERCIAL LIABILITY INSURANCE CASES

A. Cancellation of Policy

One of the most significant decisions during this survey period focuses on an insurance company's attempt to cancel a homeowners policy by certified mail, which was never claimed by the insured. In *Conrad v. Universal Fire & Casualty Insurance Co.*,[84] the Indiana Supreme Court concluded that such an attempt did not provide adequate cancellation notice to the insured.[85]

The insurance company accepted an application for homeowners insurance coverage on the insured's property.[86] However, after inspecting the property, the insurance company decided to cancel the policy; cancellation was permitted "for

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78. *See id.*

79. *Id.* at 672-74. The court summarized earlier decisions by stating:

> In sum, [*Automobile Underwriters, Inc. v. Stover*, 268 N.E.2d 114 (Ind. Ct. App. 1971)] permitted rescission based on material misrepresentations, [*American Underwriters Group, Inc. v. Williamson*, 496 N.E.2d 807 (Ind. Ct. App. 1986)] held that voiding coverage is never permissible in light of changes in the [Financial Responsibility Act, IND CODE §§ 9-25-44-1 to -11 (1998)], [*Motorists Mutual Insurance Co. v. Morris*, 654 N.E.2d 861 (Ind. Ct. App. 1995)] held that the insurer could void coverage so long as the third party victim had uninsured motorist protection, and [*Pekin Insurance Co. v. Super*, 912 F.Supp. 409 (S.D. Ind. 1995)] attempted a compromise by allowing the insurer to deny coverage only above the minimum liability amounts specified by the Act.

Id. at 672.

80. IND. CODE §§ 9-25-4-1 to -11 (1998).

81. *Colonial Penn Ins. Co.*, 690 N.E.2d at 672.

82. *Id.* at 673.

83. *See id.*

84. 686 N.E.2d 840 (Ind. 1997).

85. *Id.* at 841.

86. *See id.*

any reason" within the first sixty days. In canceling the policy, the insurance company sent notice to the insured via certified mail, with return receipt requested.[87] The notice was returned to the insurance company as "unclaimed."[88]

Subsequently, a fire occurred at the insured's property.[89] The insureds notified their insurance company and discovered their policy had been canceled. The insureds filed suit against the insurance company after their claim was denied. The insurance company argued that cancellation notice was proper and effective.[90] The trial court and the court of appeals[91] agreed with the insurance company.[92] However, the Indiana Supreme Court found use of certified mail insufficient in providing cancellation notice to an insured when the certified letter is returned undelivered.[93]

The court observed that certified mail requires the signature of the recipient.[94] Due to the growing number of families in which all adults work during mail delivery hours, it is less likely a postal worker will be able to obtain a signature.[95] Instead, the court found the use of regular mail, which was authorized by the policy as a means to send cancellation notice, is more effective in providing notice to the insured.[96] If regular mail is used and the notice is not returned, then it is presumed that the insured received the notice.[97] For the insured to prevent cancellation, he must rebut the presumption.[98]

This case demonstrates that as long as the policy authorizes its use, insurers should send cancellation notices via regular mail to create the presumption of receipt. Failure to do so may make it more difficult for the insurance company to establish that the policy was canceled.

B. General Liability Coverage for Faulty Workmanship Claim

Contractors are often sued for alleged faulty workmanship. Contractors usually purchase general liability insurance coverage and believe that it will cover all claims that may be asserted against them, including claims for faulty workmanship. However, in *R.N. Thompson & Associates, Inc. v. Monroe Guaranty Insurance Co.*,[99] an informative reading for contractors and their

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87. *See id.* The policy permitted cancellation by stating "[p]roof of mailing shall be sufficient proof of notice." *Id.* at 842.

88. *See id.* at 841.

89. *See id.*

90. *See id.*

91. 670 N.E.2d 936 (Ind. Ct. App. 1996), *reversed*, 686 N.E.2d 840 (Ind. 1997).

92. *See Conrad*, 686 N.E.2d at 841.

93. *Id.*

94. *Id.* at 842.

95. *See id.*

96. *Id.* at 843.

97. *See id.*

98. *See id.*

99. 686 N.E.2d 160 (Ind. Ct. App. 1997), *trans. denied*, 698 N.E.2d 1191 (Ind. 1998).

counsel, a general liability policy was found not to cover claims for the repair or replacement of faulty workmanship.[100]

A contractor developed and built an addition to a housing development.[101] The homeowners association sued the contractor after observing that the plywood used for the roof decking had deteriorated. The association sought damages for the cost to repair or replace the defective workmanship. The contractor's insurance companies denied the claim because it was for an economic loss and did not constitute "property damage," and it did not arise from an "occurrence" as defined by the policy.[102]

The appellate court upheld the trial court's grant of the insurance companies' Motions for Summary Judgment on a lack of coverage obligation.[103] The court first concluded that a claim for the repair and replacement of an insured's faulty workmanship does not involve "physical injury to tangible property," which is required in order for "property damage" to trigger a coverage obligation.[104] In a quote often relied upon, but still offering simple and complete analysis, the court stated:

> [T]he costs attendant upon the repair or replacement of the insured's own faulty work is part of every business venture and is a business expense to be borne by the insured-contractor in order to satisfy customers. It is a business risk long excluded by comprehensive liability policies. Another form of risk in the insured-contractor's line of work is injury to people and damage to other property caused by the contractor's negligence or defective product. It is this risk which the policy in question covers.[105]

The court also concluded that the contractor's work did not establish an "occurrence" as required by the policy.[106] The policy defined an "occurrence" in general terms as an "accident" on the part of the insured.[107] Because the homeowners association's lawsuit against the contractor was for breach of contract arising out of faulty workmanship by the contractor, the conduct at issue was not an "accident" and did not qualify as an "occurrence."[108] The court noted that a typical general liability policy "'does not cover an accident of faulty workmanship but rather faulty workmanship which causes an accident.'"[109]

This case fills a void in Indiana law concerning claims under a general liability policy for faulty workmanship. Formerly, Indiana case law addressed

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100. *Id.* at 165.
101. *Id.* at 161.
102. *See id.*
103. *Id.* at 165.
104. *Id.* at 163.
105. *Id.* at 163 (quoting Indiana Ins. Co. v. DeZutti, 408 N.E.2d 1275, 1279 (Ind. 1980)).
106. *Id.* at 165.
107. *See id.* at 164.
108. *See id.* at 165.
109. *Id.* (quoting *DeZutti*, 408 N.E.2d at 1279).

policy exclusions,[110] which presumed that an initial coverage obligation is owed until the exclusion is applied. Now, in addition to asserting that coverage is excluded under the "builders risk" exclusions contained in a policy,[111] practitioners can rely on case law establishing that no insurance coverage is owed for claims of faulty workmanship because there is no "property damage" or "occurrence" necessary to trigger coverage.

C. Coverage for Wife's Knowledge of Husband's Sexual Molestations

In *Frankenmuth Mutual Insurance Co. v. Williams*,[112] a girl was sexually molested by her babysitter's husband.[113] Initially, the girl sued only the husband, but later amended her complaint to add a claim that the wife "negligently" failed to supervise the girl during the time she was in the wife's home.[114] Because the insurance company denied coverage to the husband and wife, it did not provide any counsel to them under a reservation of rights or file any declaratory judgment action disclaiming coverage.[115]

After previously reaching the Indiana Supreme Court on other grounds,[116] the supreme court addressed whether the insurance company was collaterally estopped from denying coverage after the wife entered into a consent judgment in the victim's negligence lawsuit.[117] The insurance company argued that no coverage was available to the wife because the molestation consisted of "intentional" conduct by her husband, which is excluded under the policy.[118] However, the supreme court found that the insurance company could not allege the injuries were caused by intentional conduct because the consent judgment was based on an agreement that the wife's liability was negligent and not intentional conduct.[119]

Also, the insurance company argued that negligence occurred while the wife engaged in a "babysitting service," which is also excluded from coverage.[120] The

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110. *See DeZutti*, 408 N.E.2d at 1278).

111. The policy usually contains exclusions for "your work" or "your product" which are specifically designed for contractor situations. *See id.* at 1277.

112. 690 N.E.2d 675 (Ind. 1997).

113. *Id.* at 676.

114. *See id.* at 676-77.

115. Such alternatives are available and should be pursued by an insurance company where any uncertainty exists about the availability of coverage. *See* Liberty Mut. Ins. Co. v. Metzler, 586 N.E.2d 897, 902 (Ind. Ct. App. 1992).

116. *See* Frankenmuth Mut. Ins. Co. v. Williams, 645 N.E.2d 605, 607 (Ind. 1995) (determining that the insurance company possessed notice of the claim by receiving a subpoena for the insurance claim file and, therefore, is collaterally estopped from denying liability).

117. *Williams*, 690 N.E.2d at 678.

118. Under the policy, coverage was excluded for any injuries "caused intentionally by or at the direction of *any* insured." *Id.* at 678 (emphasis added).

119. *Id.* at 678.

120. *Id.*

supreme court reversed the summary judgment for the victim on the coverage issue, so that the insurance company could litigate that fact issue–whether the wife was engaged in a business venture.[121] The court found disputed facts which needed to be addressed by the trier of fact, and that the consent judgment did not prevent the insurance company from litigating this particular issue.[122]

This case is one of many which demonstrates the risks insurers face when they fail to seek a declaratory judgment on the issue of coverage or fail to provide an insured with a defense under a reservation of rights. Where coverage does not appear to exist, the insurer should seek a judicial declaration that no coverage exists, so that collaboration between the victim and insured cannot foreclose the insurer from pursuing its coverage defenses.

D. Sexual Harassment Claim in a General Liability Policy

An increasingly frequent situation focuses on whether coverage exists under a general liability policy for claims of sexual harassment. In *General Accident Insurance Co. of America v. Gastineau*,[123] a federal district court, interpreting specific policy language, found that such coverage existed.[124] A male employee alleged that company employees engaged in "hostile work environment" sexual harassment.[125] The company's insurer sought to deny the company's insurance claim by relying on a "co-employee" exclusion, as well as contending that no "bodily injury" or "occurrence" existed as required by the policy.[126]

The court had no difficulty disposing of the insurer's reliance upon the "co-employee" exclusion because the exclusion had been modified by an endorsement and the insurance company did not address the issue in its brief.[127] In addressing whether "bodily injury" was alleged to trigger coverage, the court found no direct allegations of physical contact to the victim.[128] However, the court believed that the simple allegation of a "hostile work environment," as a form of sexual harassment, is sufficient to allege "bodily injury" such that the insurance company should have provided coverage:

> Not every hostile work environment case necessarily involves physical contact, but we believe that bodily contact is sufficiently inherent in hostile work environment claims that, without conducting any reasonable investigation into [the plaintiff's] allegations, [the insurance company's] duty to defend [the insured] was triggered.[129]

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121. *Id.* at 681.
122. *Id.*
123. 990 F.Supp. 631 (S.D. Ind. 1998).
124. *Id.* at 638.
125. *See id.* at 634.
126. *See id.* at 632.
127. *Id.* at 633.
128. *Id.* At trial, however, the victim testified that physical contact occurred. *Id.* at 635.
129. *Id.* at 635.

The court also found that the insured established that an "occurrence" existed such that a coverage obligation was owed.[130] Specifically, the court determined that a claim for hostile work environment involved a negligence standard of conduct by the insured as opposed to an intentional standard of conduct:

> In sum, the Seventh Circuit has made clear that, in order for an employer to discriminate against an employee who objectively and subjectively has been the victim of a hostile work environment, it must have known or should have known about the discrimination. . . . Because the standard for employer liability for hostile work environment claims is negligence, we hold that [the plaintiff's] hostile work environment claim against [the insured] qualifies as an occurrence pursuant to its insurance policy.[131]

Therefore, practitioners facing a coverage question for discrimination claims must look closely to the language of the policy. While general liability policies are not designed for discrimination claims, coverage may exist if the policy does not have the appropriate exclusionary language.

E. Standards for Bad Faith by Insurer in Handling Fire Loss Claim

Since the Indiana Supreme Court established the tort of bad faith by an insurer in handling an insured's claim,[132] attorneys have been uncertain of the elements necessary to show bad faith. Unfortunately, many attorneys representing insureds have threatened to pursue bad faith actions against insurers whenever a disagreement exists between the insured and insurer.[133] Fortunately, in *Colley v. Indiana Farmers Mutual Insurance Group*,[134] the court clarified the elements necessary to show that an insurer engaged in bad faith.

A fire loss occurred at the insured's home, which was investigated by the insurer.[135] The insured contended that the insurer engaged in bad faith by concealing its arson investigation of the insured's fire loss and that the deception prevented the insured from preserving evidence to support his claim.[136] The trial court granted summary judgment to the insurer on the bad faith claim, and the insured appealed.[137]

The appellate court affirmed the trial court's summary judgment.[138] The court held that the mere negligent handling of a claim by an insurer did not

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130. *Id.* at 638.

131. *Id.*

132. *See* Erie Ins. Co. v. Hickman, 622 N.E.2d 515, 519 (Ind. 1993).

133. An insurance company possesses a right to disagree with its insured on liability or damages without committing bad faith. *Id.* at 520. *See also supra* Part I.D.

134. 691 N.E.2d 1259 (Ind. Ct. App. 1998).

135. *See id.* at 1260.

136. *See id.*

137. *See id.*

138. *Id.*

amount to bad faith.[139] Instead, the court found that the insured must show "an element of culpability" on the part of the insurer.[140] In discussing the culpability element, the court stated:

> As an example of the additional evidence needed, the Indiana Supreme Court noted that "the lack of a diligent investigation alone is not sufficient to support an award. On the other hand, for example, an insurer which denies liability knowing that there is no rational, principled basis for doing so has breached its duty."[141]

In the *Colley* case, sufficient evidence was shown of the insurer's belief that it had notified the insured it was pursuing an arson investigation.[142]

This case demonstrates the significance of "culpable" conduct on the part of the insurer to finding a bad faith action. A mere dispute or disagreement between the insured and insurer is insufficient.

F. Meaning of "Suit" and "Damages" in Environmental Claim

Hartford Accident & Indemnity Co. v. Dana Corp.[143] is a complicated case, but with important rulings by the court. Due to the complexity of the facts and issues, it is only briefly discussed in this Article. However, if faced with an environmental claim, this case is a "must read" for practitioners.

The insured manufactured automotive parts, with many of its facilities in Indiana.[144] It purchased a number of primary and excess insurance policies from different insurers.[145] Various lawsuits by government agencies and others were filed against the insured to recover environmental cleanup costs.[146] The insured submitted claims for coverage under its policies with the various insurers which were, for the most part, denied.[147] Consequently, the insured filed a declaratory judgment action seeking coverage.[148]

The appellate court addressed a number of issues. First, the court faced a choice of law question based on the national scope of the insured's operations and decided Indiana was the proper venue.[149] Secondly, the court concluded that the term "suit" as contained in the policy was ambiguous such that the

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139. *Id.* at 1261.
140. *Id.*
141. *Id.* (quoting Erie Ins. Co. v. Hickman, 622 N.E.2d 515, 520 (Ind. 1993)).
142. *See id.*
143. 690 N.E.2d 285 (Ind. Ct. App. 1997), *trans. denied*, 698 N.E.2d 1191 (Ind. 1998).
144. *See id.* at 289.
145. *See id.* at 288.
146. *See id.*
147. *See id.*
148. *See id.*
149. *Id.* at 291. The court concluded that Indiana law applied based upon the "most intimate contacts" test. *Id.*

governmental actions are covered under the primary insurers' policies.[150] The court stated, "We agree with those courts which have found coercive and adversarial administrative proceedings to be 'suits.' To decide otherwise would encourage insureds to not cooperate with governmental agencies, thus running the risk of huge fines, punitive damages, and delay in remediating environmental pollution."[151] The court also concluded that the term "damages" in a commercial general liability policy includes "[Environmental Protection Agency] or state-mandated cleanup and response costs."[152]

This case is significant in defining the scope of coverage for administrative proceedings. Most proceedings result in costly legal fees and costs and now fall within the duty to defend that exists under the policy.

III. Health and Medical Insurance

A. Subrogation Under ERISA of Uninsured Motorist Benefits

Generally, a health plan governed by the Employee Retirement Income Security Act ("ERISA")[153] creates instant uncertainty when a personal injury claim is involved. In *Southern Indiana Health Operations, Inc. ("SIHO") v. George*,[154] the court discussed what happens when an administrator of an ERISA-controlled plan seeks to subrogate for medical expenses paid on behalf of the injured participant from the participant's settlement with his insurance carrier.

In *SIHO*, the plan participant settled with his insurance carrier for $145,000 under the uninsured motorist coverage provision.[155] Upon learning of the settlement, the ERISA Plan Administrator asserted a subrogation lien against a portion of the medical expenses paid by the plan.[156] The Plan Administrator relied upon language in the plan requiring reimbursement for any recovery by the participant of amounts paid from a "third party."[157]

The trial court granted summary judgment against the Plan Administrator in his attempt to enforce the subrogation provision.[158] The appellate court discussed whether the Plan Administrator's decision that recovery of amounts paid by the insured's uninsured motorist carrier satisfied the "third party" proceeds requirement was arbitrary and capricious.[159] Based upon the plan language, the court concluded that the Plan Administrator's decision was not arbitrary and

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150. *Id.* at 296.

151. *Id.*

152. *Id.* at 298.

153. 29 U.S.C. §§1001-461 (1994 & Supp. II 1996).

154. 696 N.E.2d 476 (Ind. Ct. App. 1998).

155. *See id.* at 477.

156. The total amount of medical expenses was $70,820, but the administrator sought $46,426 after deducting its share of attorney fees and expenses. *See id.* at 477-78.

157. *See id.* at 478.

158. *See id.*

159. *Id.* at 479-80.

capricious and reversed the summary judgment.[160]

A Plan Administrator is granted a great deal of discretion in administering an ERISA plan. This case exemplifies that discretion when interpreting the subrogation rights of the plan to recover amounts paid.

B. Material Misrepresentation on Medical Insurance Policy

The decision of *Ruhlig v. American Community Mutual Insurance Co.*,[161] contains an excellent analysis of what to do when an insured makes material misrepresentations on a medical policy application. The insured submitted an application and, when asked to identify any visits with medical practitioners over a ten year period, only listed the medical treatment she received for pneumonia.[162] The applicant also authorized release of her medical records to the insurer. Based on the applicant's statements, the insurance company issued a policy to the applicant. Approximately one year after the policy was issued, the insured underwent coronary surgery and incurred costly medical expenses.[163] The insurer investigated and learned that the insured had been diagnosed, within ten years prior to her application, with chronic obstructive pulmonary disease ("COPD"), pulmonary fibrosis, and lumbar disc disease.[164]

Based on these omissions in the application, the insurer rescinded the insured's policy, refunded her premium, and refused to pay her medical expenses.[165] The insured filed a breach of contract action against the insurer and the insurer responded by filing a Counterclaim for Declaratory Judgment seeking policy rescission.[166] The insurer then filed a Motion for Summary Judgment accompanied by an affidavit from the insurer's underwriter stating that if the insurer had known of the insured's medical problems, a policy would not have been issued.[167]

The trial court granted the insurer's request for summary judgment and the insured appealed.[168] The appellate court discussed when an insurance company may successfully seek rescission based upon omissions in the application:

> False representations on an insurance application made by an insured concerning a material fact, which mislead, will void an insurance contract, just as in any other contractual relationship, regardless of whether the misrepresentation was innocently made or made with fraudulent intent. . . . A representation is material if the fact omitted or misstated, if truly stated, might reasonably have influenced the insurer

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160. *Id.* at 480.
161. 696 N.E.2d 877 (Ind. Ct. App. 1998).
162. *See id.* at 878.
163. *See id.*
164. *See id.* at 878-79.
165. *See id.* at 879.
166. *See id.*
167. *See id.*
168. *See id.*

in deciding whether to reject or accept the risk or charge a higher premium.[169]

Based upon the evidence presented by the insurance company, the court of appeals affirmed the summary judgment permitting rescission.[170] The court also rejected the insured's argument that the insurer is precluded from seeking rescission based upon its failure to discover the insured's medical condition when the name, address and phone number of her doctor is included on the application.[171] The court acknowledged that the insured could reasonably rely on the truthfulness of the insured's application and has no duty to search for inconsistencies in the application.[172]

This decision clearly allows the insurers to rely upon the statements of the insureds in acquiring coverage. It would be unreasonable to require the insurers to verify all information on all applications before issuing coverage. Instead, the doctrine of rescission still remains a viable procedure to address material misrepresentations on policy applications.

169. *Id.* at 880 (citations omitted).
170. *Id.* at 881-82.
171. *Id.* at 881.
172. *Id.*

RECENT DEVELOPMENTS IN INTELLECTUAL PROPERTY LAW

CHRISTOPHER A. BROWN*

INTRODUCTION

During the period of October 1, 1997 through September 30, 1998, several cases concerning intellectual property law were reported that are of interest to inventors, artists, lawyers, and businesses in Indiana. Patent law underwent, if not a major change, at least a rejection of the axiom that business methods are unpatentable. An Indiana federal court ruled on a relatively young provision of the Copyright Act[1] that had not been addressed before in the Seventh Circuit. The interplay of intellectual property law and the internet continues to be a topic of litigation, and the Indiana Court of Appeals weighed in with an opinion concerning jurisdiction in a case involving trademark use on the internet. Indiana courts also continued to flesh out the parameters of the Indiana Trade Secret Act.[2] These cases are the most important intellectual property cases of the past year affecting the rights and opportunities of Indiana citizens and businesses.

I. THE END OF THE "BUSINESS METHOD EXCEPTION" TO PATENTABILITY

A. Basis for the "Business Method Exception"

The Patent Act (the "Act") of the United States provides that, subject to the conditions further laid out in the Act, anyone who "invents or discovers any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof, may obtain a patent therefor . . . ."[3] Thus, the first hurdle to overcome in obtaining patent protection is to fit the thing to be patented into one of the four statutory categories: process, machine, manufacture, or composition of matter. An idea or simple printed matter in and of itself cannot be patented; to be considered for patent protection, the idea must be placed into a practical, useful form by incorporation into a proposed or actual device, product, chemical composition, or set of actions.[4]

The term "process" is defined in the Act as a "process, art or method, and includes a new use of a known process, machine, manufacture, composition of matter, or material."[5] This statutory definition indicates the generally broad

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* Associate, Woodard, Emhardt, Naughton, Moriarty & McNett. A.B., 1989, Wabash College; J.D., 1996, Indiana University School of Law—Indianapolis.

1. 17 U.S.C. §§ 101-1008 (1994 & Supp. III 1997).

2. IND. CODE §§ 24-2-3-1 to -8 (1998).

3. 35 U.S.C. § 101 (1994).

4. *See, e.g.*, Diamond v. Diehr, 450 U.S. 175, 182 (1981) (holding that "laws of nature, natural phenomena, and abstract ideas" are unpatentable subject matter); Rubber-Tip Pencil Co. v. Howard, 87 U.S. (20 Wall.) 498, 507 (1874) ("An idea of itself is not patentable, but a new device by which it may be made practically useful is.").

5. 35 U.S.C. § 100(b) (1994).

meaning of "process," which focuses on ways of accomplishing a given task or goal and uses of physical things or acts. However, in interpreting § 101 and its predecessor statutes, the case law carved out two principal "exceptions"[6] to the patentability of processes, the "mathematical algorithm" exception and the "business method" exception.[7]

The mathematical algorithm exception is effectively a restatement of the principle that abstract ideas cannot be patented. In *Diamond v. Diehr*,[8] the Court followed its earlier pronouncements in explaining that mathematical principles, equations, or computations by themselves are not patentable subject matter so long as they remain in the abstract.[9] If such algorithms are made a part of a practical application or "a useful, concrete and tangible result," then they may be patentable along with the application or result.[10] Thus, the Pythagorean formula, $a^2 + b^2 = c^2$, mathematically expresses in the abstract the dimensional relationship between the legs of a right triangle, and cannot, standing alone, be patentable subject matter. However, a surveying device, which incorporates that formula into its computations and provides a result, is subject matter for which a patent can be sought.[11]

The second exception is known as the "business method" exception. The 1908 case *Hotel Security Checking Co. v. Lorraine Co.*[12] is the seminal case stating that a system for "transacting business disconnected from the means for carrying out the system"[13] is not an art or process, and thus does not fall into a statutorily protectible category of invention. In *Hotel Security*, the court considered a claimed method "for cash-registering and account-checking"[14] intended to prevent employee theft. Even though the court also addressed the apparent lack of novelty in the claimed method, the case has been cited as precedent for declaring methods and systems of doing business to be outside the categories of patentable subject matter.[15]

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6. These doctrines are commonly called "exceptions," even though it is unclear where the authority for an exception to 35 U.S.C. § 101 arises. They are more properly thought of simply as factual situations deemed to reside outside the categories identified by § 101. Nonetheless, to conform with common usage, the term "exception" is used in this Article to refer to these doctrines.

7. *See* Diamond v. Diehr, 450 U.S. 175 (1981) (explaining the mathematical algorithm exception); Hotel Sec. Checking Co. v. Lorraine Co., 160 F. 467, 469 (2d Cir. 1908) (explaining the business method exception).

8. 450 U.S. 175 (1981).

9. *Id.* at 185. *See also* Parker v. Flook, 437 U.S. 584 (1978); Gottschalk v. Benson, 409 U.S. 63 (1972).

10. *In re* Alappat, 33 F.3d 1526, 1544 (Fed. Cir. 1994) (en banc).

11. *See* Arrythmia Research Tech., Inc. v. Corazonix Corp., 958 F.2d 1053, 1066 (Fed. Cir. 1992) (finding that a machine that performs calculations on electrocardiograph signals to convert the signals into information about heart condition is patentable subject matter).

12. 160 F. 467 (2d Cir. 1908).

13. *Id.* at 469.

14. *Id.* at 467.

15. *See* 1 DONALD S. CHISUM, CHISUM ON PATENTS § 1.03[5], at 1-75 to -76 & 1-76 n.3

B. State Street Bank & Trust Co. v. Signature Financial Group, Inc.

Both of these doctrines were reviewed by the U.S. Court of Appeals for the Federal Circuit in *State Street Bank & Trust Co. v. Signature Financial Group, Inc.*[16] Signature owned U.S. Patent No. 5,193,056, entitled "Data Processing System For Hub And Spoke Financial Services Configuration." As interpreted by the court, the patent included claims to a data processing system comprised of a computer processor, data storage, and several arithmetic logic circuits configured to perform operations on and store mutual fund data such as asset amounts, income, expenses, and gain or loss.[17] The appellate court noted that the patent claims were directed to a machine, but that it mattered little whether the claims were machine claims or process claims because both categories are listed in § 101.[18]

State Street had brought a declaratory judgment action seeking, among other remedies, the invalidation of Signature's patent. On State Street's motion for summary judgment, on the ground that the patent claims did not define subject matter encompassed by § 101, the district court ruled that the patent's claims delineated a mathematical algorithm that was not "applied to or limited by physical elements or process steps."[19] The district court also stated that the patent's subject matter fell within the business method exception.[20] Accordingly, summary judgment of invalidity was granted in favor of State Street.[21]

On appeal, the Federal Circuit began by examining § 101. That provision's "plain and unambiguous meaning" is that anything falling within a § 101 category is appropriate subject matter for a patent.[22] Indeed, the court found that the wording of § 101 indicates that Congress' intent was not to restrict the subject matter for which patents may be sought, except as specifically provided in § 101.[23] This short but powerful opening foretold the court's view of non-statutory "exceptions" to patentable subject matter, and in the author's view is part of a continuing trend by the Federal Circuit of articulating bright-line standards for potentially gray areas of the patent laws.

The *State Street* court then turned its attention to the mathematical algorithm exception. It noted that the district court's analysis incorporated a test known as

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(Matthew Bender, 1997).

16. 149 F.3d 1368 (Fed. Cir. 1998).

17. *Id.* at 1371-72.

18. *Id.*

19. State St. Bank & Trust Co. v. Signature Fin. Group, Inc., 927 F. Supp. 502, 513-15 (D. Mass. 1996).

20. *Id.* at 515-16.

21. *See id.* at 517.

22. *State St. Bank & Trust*, 149 F.3d at 1372.

23. *Id. Accord* Diamond v. Diehr, 450 U.S. 175, 182 (1981); Diamond v. Chakrabarty, 447 U.S. 303, 309 (1980) (finding Congress intended that § 101 reach "anything under the sun that is made by man").

the Freeman-Walter-Abele test to identify whether particular subject matter fell within § 101.[24] Citing *In re Alappat*, *Diamond v. Diehr*, and *Diamond v. Chakrabarty*, the Federal Circuit took the opportunity to discard explicitly the Freeman-Walter-Abele test as potentially misleading.[25] Insofar as the test looks for mathematical algorithms at the outset, it could cause a rejection of machines or processes employing the algorithm as unpatentable subject matter, even if the machine or process produces the "useful, concrete and tangible result."[26] *Alappat* identifies as the hallmark of patentable subject matter.

Consequently, the *State Street* court shifted the focus of a § 101 inquiry from an attempt to shoehorn a given invention into one of the four categories of § 101. Instead, "[t]he question of whether a claim encompasses statutory subject matter should . . . focus . . . on the essential characteristics of the subject matter, in particular, its practical utility."[27] The implication is that any subject matter showing a practical utility—i.e., providing a useful, concrete, and tangible result—is proper subject matter for a patent. With respect to the Signature patent, the court found that the claimed system produced such a result by transforming financial data via mathematical calculations into a final share price.[28] The final share price was recorded and reported to *interested* parties, apparently including regulatory authorities. Because it produced that useful result, the Federal Circuit reasoned, the system constituted statutory subject matter under § 101, and if it were to pass the remaining conditions for patentability, it could be protected by a patent.[29]

Having found that the Signature patent was not an unpatentable abstract idea, the court then approached the alternative basis for invalidating the Signature patent, that the patent claimed an unpatentable method of doing business.[30] After reviewing several cases commonly cited as support for the business method exception, the *State Street* court found that neither the Federal Circuit nor its predecessor, the Court of Customs and Patent Appeals, had used the exception

24. *State St. Bank & Trust*, 149 F.3d at 1373-74. The court expressed the Freeman-Walter-Abele test as:

> First, the claim is analyzed to determine whether a mathematical algorithm is directly or indirectly recited. Next, if a mathematical algorithm is found, the claim as a whole is further analyzed to determine whether the algorithm is "applied in any manner to physical elements or process steps," and, if it is, "passes muster under § 101."

Id. (citing *In re* Abele, 684 F.2d 902 (C.C.P.A. 1982); *In re* Pardo, 684 F.2d 912, 915 (C.C.P.A. 1982); *In re* Walter, 618 F.2d 758 (C.C.P.A. 1980); *In re* Freeman, 573 F.2d 1237 (C.C.P.A. 1978)).

25. *Id.* at 1374.

26. *Id.* at 1375.

27. *Id.*

28. *Id.* at 1373.

29. *See id.* at 1375.

30. *Id.*

to hold an invention unpatentable.[31] Rather, cases such as *In re Howard*,[32] *In re Schrader*,[33] *In re Maucorps*,[34] and *In re Meyer*[35] rested their holdings of unpatentability on findings that the invention at issue was an abstract idea, lacked novelty, or was obvious.[36] Even the *Hotel Security* case, as noted above, addressed the apparent lack of novelty in the patented method, and the *State Street* court interpreted *Hotel Security* to turn not on the business method exception, but on principles of novelty or lack of invention.[37]

The *State Street* court determined that the case before it fit into the same class as those prior cases. The district court's "primary reason for finding the patent invalid under the business method exception" consisted of a finding that the patented invention is claimed broadly enough to prevent use of "'virtually any computer-implemented accounting method necessary to manage'"[38] the given financial structure. This reasoning, which emphasizes the breadth of the claims, is not a judgment under § 101, but is instead part of the analysis concerning other conditions for patentability—novelty, nonobviousness, and proper specification.[39] Even the Patent and Trademark Office, in its Manual of Patent Examining Procedure ("MPEP") and Examination Guidelines for Computer Related Inventions, has acknowledged that the business method exception is no longer viable and that any claims that might be characterized as business methods should be analyzed in the same manner as any other process claims.[40] Accordingly, the Federal Circuit officially rejected any further use of the business method exception, stating that business methods are "subject to the same legal requirements for patentability as any other process or method."[41] Specifically the *State Street* court held that

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31. *Id.*

32. 394 F.2d 869 (C.C.P.A. 1968).

33. 22 F.3d 290 (Fed. Cir. 1994).

34. 609 F.2d 481 (C.C.P.A. 1979).

35. 688 F.2d 789 (C.C.P.A. 1982).

36. *See State St. Bank & Trust*, 149 F.3d at 1375-76.

37. *Id.* at 1376.

38. *Id.* at 1376-77 (citing State St. Bank & Trust Co. v. Signature Fin. Group, Inc., 927 F. Supp. 502, 516 (D. Mass. 1996)).

39. *See id.* Section 102 of the Patent Act delineates the criteria for the novelty condition that an invention must meet to qualify for a patent. 35 U.S.C. § 102 (1994). Section 103 provides that a patent is not available for subject matter which "as a whole would have been obvious at the time the invention was made to a person having ordinary skill in the art to which the subject matter pertains." *Id.* § 103(a). Section 112 identifies the necessary elements to be included in a patent specification. *Id.* § 112.

40. *See State St. Bank & Trust*, 149 F.3d at 1377 (citing PATENT AND TRADEMARK OFFICE, U.S. DEP'T OF COMMERCE, MANUAL OF PATENT EXAMINING PROCEDURE § 706.03(a) [hereinafter MPEP]; Examination Guidelines for Computer Related Inventions, 61 Fed. Reg. 7478, 7479 (1996)). The 1996 edition of MPEP § 706.03(a) eliminated a passage in prior editions permitting the rejection of claims based on the business method exception.

41. *State St. Bank & Trust*, 149 F.3d at 1375.

> the transformation of data, representing discrete dollar amounts, by a machine through a series of mathematical calculations into a final share price, constitutes a practical application of a mathematical algorithm, formula, or calculation, because it produces "a useful, concrete and tangible result"—a final share price momentarily fixed for recording and reporting purposes and even accepted and relied upon by regulatory authorities and in subsequent trades.[42]

Although restating and clarifying earlier opinions of the Supreme Court and the Federal Circuit, *State Street* appears to have opened the possibility of patent protection to a range of inventions previously thought by many to have been unpatentable. Practically any transformation of data that produces a useful result, particularly if embodied in computer equipment or other devices, has seemingly been given the green light for patenting. However, the method or device that transforms data must still meet the criteria of sections 102 and 103 of the Patent Act—novelty and unobviousness. Thus, hardware that calculates the area under a given curve may be patentable subject matter under *State Street*, but may not be novel or non-obvious over the calculus. Nevertheless, many businesses, particularly those like State Street that process a great deal of data, may wish to examine their data transforming methods and devices for possible patent protection.

II. Internet Jurisdiction in Indiana

As with many other areas of law, the proliferation of the internet has affected intellectual property law. Generally speaking, the internet has not appreciably affected the substance of patent, trademark, copyright, or trade secret law. An original manuscript fixed in a tangible medium of expression is still entitled to copyright protection whether that medium is a book or computer, and a trademark still identifies the source of goods or services whether that trademark is in the newspaper or on a web site.

Nonetheless, interesting challenges to intellectual property owners have arisen as they move to protect their rights against alleged infringers who use the internet. Perhaps that effect is most keenly felt in the trademark realm, as commerce on the internet becomes more widespread and easy to use. Cases have been reported in other jurisdictions that begin to address the interplay between trademark law and the registration of internet domain names.[43] These issues will

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42. *Id.* at 1373.

43. *See, e.g.*, Intermatic Corp. v. Toeppen, 947 F. Supp. 1227 (N.D. Ill. 1996); Panavision, Inc. v. Toeppen, 945 F. Supp. 1296 (C.D. Cal. 1996), *aff'd*, 141 F.3d 1316 (9th Cir. 1998). Briefly, these cases stand for the general proposition that registration of a domain name that is the trademark of another, combined with the offer to sell the domain name to the trademark owner, is an infringement of the owner's trademark rights. A "domain name" is a character set that identifies a particular computer, or "server," on the internet. For example, in the internet address *www.uspatent.com*, "www" identifies the World Wide Web, "com" identifies the top-level domain

continue to find their way before state and federal judges as the importance and availability of electronic commerce increases.

At a more basic level, however, is the question of where a lawsuit based on intellectual property improperly placed or used on the internet may be brought. If an alleged infringer or unfair competitor is located in one jurisdiction, the internet service provider (i.e. the primary physical location of the allegedly infringing data) in another, the complaining plaintiff in a third, and consumers or other parties downloading the allegedly infringing data still in other places, it is often difficult to determine a proper venue for the lawsuit. The Indiana Court of Appeals has now weighed in on the issue of jurisdiction in an internet trademark case, *Conseco, Inc. v. Hickerson*.[44]

Conseco involved a suit filed by an insurance company alleging trademark dilution, trademark infringement, commercial disparagement, and other claims against Hickerson, a resident of Texas. As the trustee of an estate, Hickerson promulgated a web site that sought information of "fraud or other evidence of unfair treatment" by Philadelphia Life Insurance Company, a subsidiary of Conseco, or any other Conseco subsidiaries, apparently to assist him in a lawsuit against Philadelphia Life.[45] The web site included the term "Conseco Inc.," in which Conseco claimed trademark rights, and also included a link enabling the reader to send electronic mail to Hickerson.[46] According to the court, the web site "did not advertise or offer any product, or seek any money."[47]

Procedurally, Conseco obtained a temporary restraining order and a date for a preliminary injunction hearing.[48] Hickerson filed a response, and the trial court held a hearing concerning the injunction.[49] With the permission of the trial court, Hickerson filed a brief after the hearing disputing the court's jurisdiction over him, and the court found that it did not have personal jurisdiction in the case.[50] Conseco appealed.

The court of appeals discussed only one of the issues Conseco raised in its appeal: "Whether Hickerson's use of Conseco's trademarked name in his web site was sufficient to support personal jurisdiction in Indiana."[51] Conseco's argument was based on the "effects test" of personal jurisdiction outlined in *Calder v. Jones*[52] and applied in a trademark case by the Seventh Circuit in

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(here, commercial), and the domain name is "uspatent." *See Panavision*, 141 F.3d at 1318.

44. 698 N.E.2d 816 (Ind. Ct. App. 1998). The court noted that the issue it faced "appears to be a question of first impression in Indiana." *Id.* at 818.

45. *See id.* at 817.

46. *See id.*

47. *Id.*

48. *See id.* at 817-18.

49. *See id.* at 818.

50. *Id.* The opinion is not clear as to whether an objection to personal jurisdiction was made at the time Hickerson filed his response or (apparently) attended the injunction hearing.

51. *Id.*

52. 465 U.S. 783 (1984).

Indianapolis Colts, Inc. v. Metropolitan Baltimore Football Club, Inc.[53] Conseco also relied on two recent cases specifically concerning personal jurisdiction in the context of internet usage, *EDIAS Software International v. BASIS International, Ltd.*[54] and *Panavision International, L.P. v. Toeppen.*[55] Conseco argued that the effects test as applied in the latter two cases supported the exercise of personal jurisdiction in Indiana over the Texas resident Hickerson.

The court of appeals, however, disagreed. After reviewing the standards for personal jurisdiction in Indiana,[56] the court discussed and distinguished *Indianapolis Colts*, *EDIAS*, and *Panavision*. *Indianapolis Colts* concerned the defendant's use of the trademark "Colts" in connection with its professional football team. Although the defendant's contacts with Indiana were tenuous, the Seventh Circuit found that an Indiana federal court had jurisdiction over the defendant, basing its finding on the existence of national television broadcasts that could reach Indiana, and apparently also on the fact that, since the trademark owner was in Indiana and did considerable business under its trademark in Indiana, the effect of the trademark infringement would be primarily felt in Indiana.[57] In a single sentence, the *Conseco* court dismissed the *Indianapolis Colts* opinion as not considering "the unique question of personal jurisdiction through the Internet."[58] With that sentence, the court apparently elected not to visit the question of whether the situs of the trademark owner or the situs of a substantial portion of the business transacted in connection with the trademark has any bearing on personal jurisdiction, choosing instead to focus exclusively on the internet flavor of the case.[59]

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53. 34 F.3d 410 (7th Cir. 1994).

54. 947 F. Supp. 413 (D. Ariz. 1996).

55. 141 F.3d 1316 (9th Cir. 1998).

56. *Conseco*, 698 N.E.2d at 818 (citing IND. R. TRIAL P. 4.4(A); Yates-Cobb v. Hays, 681 N.E.2d 729 (Ind. Ct. App. 1997); Harold Howard Farms v. Hoffman, 585 N.E.2d 18 (Ind. Ct. App. 1992)).

57. *Indianapolis Colts*, 34 F.3d at 411-12.

58. *Conseco*, 698 N.E.2d at 818.

59. It would appear that, assuming *Indianapolis Colts* to be an accurate reflection of Indiana law concerning personal jurisdiction, there are two ways to interpret the court of appeals' quick distinction of the case. First, the court may not have wanted to consider a "site of injury" inquiry given a medium that potentially reaches to all points of the globe. Such a test for personal jurisdiction would probably have to presuppose a "constructive notice" to the defendant of the plaintiff's location(s) for the "traditional notions of fair play and substantial justice" of *International Shoe Co. v. Washington*, 326 U.S. 310 (1945), and its progeny to be satisfied. Second, the court may be implicitly distancing itself from *Indianapolis Colts* and the idea that the situs of trademark injury can support jurisdiction. In that event, *Indianapolis Colts* is implicitly called into question to the extent it interprets Indiana law. The latter position appears to the author to be the correct one at this point insofar as the court did not discuss the effect of the site of the alleged trademark injury on personal jurisdiction at all, either positively or negatively. Which of these or other positions on *Indianapolis Colts* is held by Indiana courts may be delineated at a future date.

The court then turned to the two federal district court cases specifically considering the internet. *EDIAS*, in the court's view, was distinguishable "because the *EDIAS* court did not rely solely upon the 'effects test' to find personal jurisdiction."[60] Rather, in *EDIAS* the defendant, in addition to making allegedly defamatory remarks on its web site, sent electronic mail, telephone calls, and faxes into Arizona and sold merchandise in Arizona, all of which contributed to the assertion of jurisdiction over the defendant.[61] The *Conseco* court, in a situation where no other such contacts were present, found *EDIAS* not germane.[62]

The second federal case, *Panavision*,[63] concerned a so-called "cyber pirate" who had registered as a domain name trademarks belonging to the plaintiff, a California corporation. The defendant, an Illinois resident, then demanded a price for releasing the domain names to the plaintiff. The *Panavision* court found that personal jurisdiction existed over the defendant in California because the defendant aimed his "scheme to extort money" at a corporation located in California.[64] Observing that the *Panavision* court relied on the defendant's "purposefully aiming his extortion scheme" at California, the *Conseco* court distinguished *Panavision* because no actions were directed at Indiana in the case before it.[65] Notably, the court mentioned the *Panavision* court's apparent dictum that "simply registering a corporation's trademark as a domain name and posting a web site would not be sufficient to support personal jurisdiction over a non-resident defendant."[66] Nevertheless, the *Conseco* court did not rely on *Panavision* to any obvious degree it its ultimate ruling.

The court elected instead to follow the guidance of a different Ninth Circuit case, *Cybersell, Inc. v. Cybersell, Inc.*[67] *Cybersell* involved facts much closer to those in *Conseco*. An Arizona corporation sued a Florida corporation in Arizona, alleging trademark infringement by improper use of the Arizona corporation's name on the Florida corporation's web site. The web site including an Arizona corporation's name was the only contact the Florida corporation had with the state of Arizona. Further, the Arizona and Indiana long-arm statutes both extend personal jurisdiction to the extent due process allows.[68] As in *Cybersell*, the *Conseco* court found that personal jurisdiction over Hickerson did not exist.[69]

In doing so, the court listed two factors used in a personal jurisdiction analysis involving an interactive web site: (1) "the level of interactivity of the

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60. *Conseco*, 698 N.E.2d at 819.
61. EDIAS Software Int'l v. BASIS Int'l, Ltd., 947 F. Supp. 413, 417 (D. Ariz. 1996).
62. *Conseco*, 698 N.E.2d at 819.
63. Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316 (9th Cir. 1998).
64. *Id.* at 1327.
65. *Conseco*, 698 N.E.2d at 819.
66. *Id.* (citing *Panavision*, 141 F.3d at 1322).
67. 130 F.3d 414 (9th Cir. 1997).
68. *See Conseco*, 698 N.E.2d at 820.
69. *Id.*

site,"[70] and (2) the "commercial nature of the information exchange."[71] Evidently addressing the first factor, the court referred again to the *Cybersell* opinion for the proposition that "something more" than just an internet advertisement would be required before personal jurisdiction could be acquired over the web site creator or owner.[72] The "something more" must indicate that the defendant "directed his activity in a substantial way to the forum state,"[73] and will probably be satisfied by telephone calls, electronic mail, regular mail, merchandise, or advertisements specifically sent into the proposed forum state.[74] Because none of these additional contacts were present, the *Conseco* court affirmed the trial court's finding of no personal jurisdiction over Hickerson.[75]

Perhaps the most interesting statement in the *Conseco* opinion is that the effects test is

> not readily applicable in cases involving national or international corporations and the Internet. The "effects test" does not apply with the same force to a corporation as it does to an individual because a corporation's harm is generally not located in a particular geographic location as an individual's harm would be.[76]

The first portion of the statement clearly articulates that the court is concerned with the category of cases having two components: corporations and the internet. The remainder of the statement, and indeed the rest of the court's paragraph rejecting the effects test, does not refer at all to the internet. Rather, the court reasons that the national or multi-national character of a corporation means that injury to it would be felt wherever the corporation is present, instead of where the corporate headquarters is located.[77] The implicit statement is that this result would impermissibly enlarge personal jurisdiction. That reasoning would seem to apply regardless of whether the internet is the instrument used to inflict injury. Insofar as the court's declared position on the effects test represents a basis for

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70. *Id.*

71. *Id.* (citing *Cybersell*, 130 F.3d at 418; Zippo Mfg. Co. v. Zippo Dot Com, Inc., 952 F. Supp. 1119, 1124 (W.D. Pa. 1997)). The court remarked specifically that it was making the assumptions for purposes of the appeal that Hickerson's web site was interactive and that it was commercial in nature. *Id.* at 820 nn. 6-7.

72. *Id.* (citing *Cybersell*, 130 F.3d at 430).

73. *Id.* (citing *Cybersell*, 130 F.3d at 430; Blumenthal v. Drudge, 992 F. Supp. 44, 56 (D.D.C. 1998)).

74. *See id.* ("In the present case . . . Hickerson did not direct any advertising, send any e-mails or letters, or make any phone calls to Indiana."); *see also* Panavision Int'l, L.P. v. Toeppen, 141 F.3d 1316, 1322 (9th Cir. 1998).

75. *Conseco*, 698 N.E.2d at 820.

76. *Id.* at 819.

77. *Id.* at 819-20. This passage of the opinion seems to be a clearer, although still unstated, rejection of *Indianapolis Colts* to the extent that the latter stands for the proposition that personal jurisdiction exists in the forum encompassing the headquarters of a corporation alleging trademark injury. *See supra* note 59.

the court's decision to follow *Cybersell* in this case, it should be regarded as a precedential statement.

Further analysis reveals several additional points that may require resolution in future cases. In its opinion, the court left open the question of whether either of the two identified "internet jurisdictional" factors is necessary or sufficient to a finding that personal jurisdiction exists. Next, in considering what constitutes the "something more" above an internet web site or advertisement that is needed to establish jurisdiction, the court recited the subjective standard from *Cybersell*.[78] The "something more" must indicate that the defendant directed actions "in a substantial way" toward the proposed forum.[79] In the context of the well-known "minimum contacts" analysis in federal and Indiana personal jurisdiction jurisprudence, perhaps "substantial way" has a meaning the same as or similar to "minimum contacts." On the other hand, it is possible that the phrase will be interpreted as an additional component in determining personal jurisdiction. Third, the court did not address to any degree whether, in considering the commercial nature of the information exchange, the consideration is relative or absolute. In other words, it is not clear whether the court will consider a web site as having any commercial elements to meet the second factor, or that a threshold level of commercial-relatedness must exist to trigger jurisdiction.

III. INDIANA TRADE SECRET LAW AFTER *AMOCO*

In 1993, the Indiana Supreme Court decided *Amoco Production Co. v. Laird*,[80] which was one of its first pronouncements on the Indiana Uniform Trade Secrets Act ("IUTSA").[81] The *Amoco* court interpreted and applied the statutory term "not being readily ascertainable" to determine whether given information was a trade secret,[82] and thereby somewhat clarified the parameters of trade secret protection. In *Hydraulic Exchange and Repair, Inc. v. KM Specialty Pumps, Inc.*,[83] the Indiana Court of Appeals applied the *Amoco* decision when it considered whether customer and pricing information qualified as a trade secret.[84] The court also considered the breadth of an injunction against trade secret misappropriation.[85]

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78. *Conseco*, 698 N.E.2d at 820.

79. *Id.*

80. 622 N.E.2d 912 (Ind. 1993).

81. IND. CODE §§ 24-2-3-1 to -8 (1998). The IUTSA defines a trade secret as information that "[d]erives independent economic value, actual or potential, from not being generally known to, and *not being readily ascertainable by proper means* by, other persons who can obtain economic value from its disclosure or use" and is the subject of reasonable efforts to maintain its secrecy. *Id.* § 24-2-3-1 (emphasis added).

82. *Amoco*, 622 N.E.2d at 919.

83. 690 N.E.2d 782 (Ind. Ct. App. 1998).

84. *Id.* at 784-86.

85. *Id.* at 786-88.

The facts of *Hydraulic Exchange* are not uncommon among trade secret cases. As part of its lubrication business, KM daily updated its customer and pricing information, such as the names of contacts at its customers' locations and its overhead information. KM considered such information confidential. KM provided customer names, contact names, and customer sales histories to its salesperson, Titzer, for use in the course of his sales efforts on behalf of KM.[86] KM had a two-year non-competition agreement with Titzer, which provided that Titzer would not sell pumps and lubrication in geographic areas in which he sold or made sales calls on behalf of KM, and would not directly or indirectly solicit KM's customers or accounts. The court noted that the non-competition agreement also provided that an injunction was available as a remedy for breach of the agreement.[87]

About one month after resigning from KM, Titzer was hired as a sales representative by Hydraulic Exchange, a business that repaired hydraulic components and performed lubrication work. Hydraulic Exchange had done lubrication work for several clients who were also clients of KM.[88] KM sued Hydraulic Exchange and Titzer on trade secret and other grounds after it discovered that Titzer called upon one of the companies' mutual customers, and after Titzer stated to a KM officer that "he would not turn down any work that came to him."[89] On KM's motion, the trial court issued a preliminary injunction prohibiting the defendants from offering pumps or lubricant systems to KM customers, interfering with KM's employees or agreements between KM and other parties, and using or disclosing KM trade secrets "or other proprietary information or pricing information."[90] Hydraulic Exchange then filed an interlocutory appeal.

Judge Najam first considered Hydraulic Exchange's claim that the customer and pricing information at issue was not entitled to trade secret protection. He cited a provision of the IUTSA[91] and the court's prior opinion in *Ackerman v. Kimball International, Inc.*[92] in identifying four "characteristics" of a trade secret: "(1) information, (2) which derives independent economic value, (3) is not generally known, or readily ascertainable by proper means by other persons who can obtain economic value from its disclosure or use, and (4) the subject of efforts reasonable under the circumstances to maintain its secrecy."[93] In spite of its four-element formulation, the court did not specifically discuss the first or second elements as it reviewed the trade secret status of KM's customer and pricing information. It is not difficult to see that such materials constitute

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86. *See id.* at 784.

87. *Id.*

88. *See id.* at 784-85.

89. *Id.* at 784.

90. *Id.* at 785.

91. IND. CODE § 24-2-3-2 (1998).

92. 634 N.E.2d 778 (Ind. Ct. App. 1994), *vacated in part, adopted in part*, 652 N.E.2d 507 (Ind. 1995).

93. *Hydraulic Exchange*, 690 N.E.2d at 785-86.

"information." The court did not explicitly review the fourth element either, but noted evidence that KM informed employees as to confidentiality and backed-up the information from the computer system, storing it in a safe.[94] Consequently, it is not surprising that the court focused its attention elsewhere.

However, the court either lumped the second and third elements together in its analysis, or chose to ignore the element of independent economic value. Relying on the declaration in *Amoco* that "'where the duplication or acquisition of alleged trade secret information requires a substantial investment of time, expense, or effort, such information may be found "not being readily ascertainable" so as to qualify for protection,'"[95] the court found that KM had protectible trade secret information.[96] Hydraulic Exchange argued that the customer information was readily ascertainable because the "discrete market" for the two companies' goods and services would permit any competitor in the market to obtain information on potential customers "through the telephone book."[97] On one hand, the court agreed that KM's customer list itself is not a trade secret.[98] On the other hand, the court decided that, because KM's accumulation of information included more than customer names,[99] under the *Amoco* rule "KM's effort of compiling its customer and pricing information is entitled to protection even if the customer names may generally be known."[100]

The *Hydraulic Exchange* opinion seems implicitly to view both the second and third trade secret elements as addressed by that rule. While the opinion does not separately consider those elements, the second element, "deriving independent economic value," may be addressed by simply inferring that a compilation of information would have an independent economic value if for no other reason than resources would have to be spent to duplicate it.[101] Further, it is evident that the third element, "not being readily ascertainable," was addressed by the court because of its reliance on *Amoco*. However, *Hydraulic Exchange* does not necessarily stand for the principle that a compilation of available information may be "not readily ascertainable" under the IUTSA because the case dealt with information over and above available customer names. Nevertheless, the language of the opinion seems to provide support that available information accumulated or organized and kept secret can be a protectible trade secret.

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94. *Id.* at 786.

95. *Id.* (quoting Amoco Prod. Co. v. Laird, 622 N.E.2d 912, 919 (Ind. 1993)).

96. *Id.*

97. *Id.*

98. *Id.*

99. "The customer and pricing information that KM claims as a trade secret includes profits, sales, and special suppliers that are specific to each customer." *Id.*

100. *Id.*

101. The *Hydraulic Exchange* opinion noted that *Amoco* held that information may be found "not readily ascertainable" if duplicating or procuring the information would require a substantial amount of time, expense, or effort. *Id.* In such a case, it is clear that such information has independent economic value.

The court's principal holding on the first issue was that "KM's effort of compiling its customer and pricing information is entitled to protection even if the customer names may generally be known."[102] This statement of the law, while appealing from the standpoint of protecting business effort and investment, appears to the author to be somewhat awkward. The IUTSA specifically identifies "information" as the subject matter it protects, rather than a person's effort, diligence, or "sweat of the brow."[103] Certainly, a compilation of data is "information," and the compiler's effort in accumulating and preparing the compilation is indicative of the availability or ascertainability of the compilation. However, the precept that the effort of compiling information is protectible under the IUTSA does not necessarily follow from the language of the act.

The second issue addressed by the court was the breadth of the injunction issued by the trial court.[104] The court's discussion began by acknowledging that trade secret misappropriation requires not only non-consensual use or disclosure of trade secrets, but also an element of impropriety.[105] In this case, the court characterized that impropriety as Hydraulic Exchange's knowledge or reason to know that the trade secrets came from Titzer, who owed a duty of secrecy to KM through his non-competition agreement.[106] KM did not establish that Hydraulic Exchange received KM's customer and pricing information from Titzer or that Hydraulic Exchange knew of the non-competition agreement between KM and Titzer. KM did show that Hydraulic Exchange used Titzer "in preparing bids for customers that Titzer had as clients when he worked at KM."[107]

The court found that using Titzer to prepare such bids would support the inference that KM's customer and pricing information could be used to Hydraulic Exchange's benefit and KM's detriment.[108] Because threatened trade secret misappropriation may be enjoined,[109] the preliminary injunction against Hydraulic Exchange's use or disclosure of KM's information when preparing bids was upheld.[110] As noted above, however, the injunction went considerably further, including prohibitions on Hydraulic Exchange and Titzer from offering certain goods "*to any customer or client of KM* [and] . . . *[u]sing or disclosing any trade secret or other proprietary information or pricing information of KM*."[111]

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102. *Id.*

103. *See* Feist Publications, Inc. v. Rural Tel. Serv., Inc., 499 U.S. 340, 363-64 (1991) (holding that the Federal Copyright Act does not protect the effort or "sweat of the brow" of one who collects and publishes information, but protects only the person's expression of the information).

104. *Hydraulic Exchange*, 690 N.E.2d at 786.

105. *Id.* at 787.

106. *Id.*

107. *Id.*

108. *Id.*

109. *See* IND. CODE § 24-2-3-3 (1998).

110. *See Hydraulic Exchange*, 690 N.E.2d at 787.

111. *Id.* at 788 (emphasis added).

Those provisions of the preliminary injunction were determined to be overbroad.[112] The trade secrets at issue were KM's "customer and pricing information," not the customer names themselves. Accordingly, relief that enjoins business contact with KM's customers, without regard to whether any of the "customer and pricing information" was used in the contact, does not have a proper connection to the trade secrets, and therefore to the threatened misappropriation. In Judge Najam's words, the injunction "should be limited to those solicitations made by [Hydraulic Exchange] in which [it] might utilize KM's trade secrets including, specifically, transactions in which Titzer participates, directly or indirectly."[113] This aspect of the *Hydraulic Exchange* opinion highlights an obvious consideration in trade secret litigation, the importance for the plaintiff of defining and proving trade secret misappropriation as broadly as possible.

IV. *Martin v. Indianapolis*—Copyright Damages

One other Indiana case decided in the past year deserves mention because it considered damages in a copyright-related action. *Martin v. Indianapolis*[114] was a case of first impression in the Seventh Circuit, and was one of the first cases in the nation concerning the Visual Artists Rights Act ("VARA").[115] In October 1997, Martin won summary judgment on his claim that the City of Indianapolis infringed his rights under VARA by destroying a sculpture he created.[116] At that time, the court reserved its final ruling and directed the parties to present arguments as to the level of damages. The *Martin* opinion reviewed those arguments and decided the remedies to be awarded.

VARA was enacted in 1990 to bring U.S. copyright law further into agreement with international copyright law. Among other terms, VARA provides that

> the author of a work of visual art . . . subject to the limitations set forth in section 113(d), shall have the right—(A) to prevent any intentional distortion, mutilation, or other modification of that work which would be prejudicial to his or her honor or reputation, and any intentional distortion, mutilation, or modification of that work is a violation of that right, and (B) to prevent any destruction of a work of recognized stature, and any intentional or grossly negligent destruction of that work is a violation of that right.[117]

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112. *See id.*

113. *Id.*

114. 4 F. Supp. 2d 808 (S.D. Ind. 1998).

115. 17 U.S.C. § 106A (1994). VARA is codified among and is related to provisions of the Copyright Act, 17 U.S.C. §§ 101-1008 (1994 & Supp. III 1997).

116. *See Martin*, 4 F. Supp. 2d at 809.

117. 17 U.S.C. § 106A(a)(3) (1994). The exceptions in § 113(d) concern works of visual art incorporated or made part of a building. *Id.* § 113(d).

The provision applies to a "work of visual art," which is generally defined as a painting, print drawing, sculpture, or still photograph produced for exhibition, existing in a single copy or a limited edition.[118] Further, it is the "author" of the work, not the owner of a copy or of the premises where the copy is situated, whose rights are protected by VARA.[119] Thus, business owners, public entities, and others who own or display works of visual art must remain cognizant of the author's right to the maintenance of the quality of his or her works.

After Indianapolis was adjudged to have violated VARA, Martin requested statutory damages under the Copyright Act as well as costs and attorney fees.[120] Martin contended that Indianapolis' (the "City's") actions were willful, and therefore supported enhanced statutory damages of $100,000.[121] Not surprisingly, the City countered that it did not act willfully, as that term is used in the Copyright Act, entitling Martin to only $20,000 in statutory damages, and that Martin was not entitled to full costs or fees.[122]

Judge Barker first considered the meaning of "willfulness," noting that the term is not defined in the Copyright Act.[123] Citing both the Nimmer treatise[124] and *Wildlife Express Sales Corp. v. Carol Wright Sales, Inc.*,[125] the judge decided that willfulness requires the infringement defendant to know or have reason to know that his or her "actions constituted infringement, whether through past infringement activity and lawsuits or direct notice from the plaintiff or some other acceptable form of notice."[126] That the defendant's actions are intentional, i.e., that the defendant's purpose was to cause the action or consequence that was caused, is not sufficient to establish willfulness. In the copyright realm, to prove willfulness a plaintiff must show that the defendant was on notice that its actions amount to a copyright infringement.[127]

In *Martin*, the plaintiff showed that the City knew of his "contractual rights and ownership rights" in the work, but failed to show that the City knew of his VARA rights, and thus the City was not liable for enhanced statutory damages.[128] This is at least one instance in which ignorance of the law may be an excuse. In pointing out the insufficiency of his case, the court particularly noted that Martin did not assert "that the City knew about the existence of VARA."[129] The court

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118. *See id.* § 101.

119. *Id.* § 106A.

120. *See Martin*, 4 F. Supp. 2d at 809; *see also* 17 U.S.C. §§ 504(c) & 505 (1994).

121. *See Martin*, 4 F. Supp. 2d at 809.

122. *See id.* at 810.

123. *Id.*

124. 4 MELVILLE B. NIMMER & DAVID NIMMER, NIMMER ON COPYRIGHT § 14.04[B][3], at 14-59 (Matthew Bender, 1998).

125. 18 F.3d 502 (7th Cir. 1994).

126. *Martin*, 4 F. Supp. 2d at 810.

127. *See id.* (discussing what constitutes notice).

128. *See id.* at 811.

129. *Id.*

proceeded to award the maximum amount of non-enhanced statutory damages based primarily on the fact that Martin's work had been subjected to "the most extreme form of copyright infringement possible: total destruction."[130] The court also noted that even though the City had not willfully infringed, its proven disregard for the work and Martin's statutory rights in it further justified such an award.[131]

The court then moved on to Martin's claim for costs and attorney's fees. Quoting the Copyright Act, Judge Barker acknowledged that such an award may be made in the court's discretion.[132] She also rejected the City's argument that the case counseled against awarding costs and fees because it encompassed "a novel and complex area of copyright law."[133] Rather, while case law concerning VARA is relatively "undeveloped," in the court's words, guidance was found in *Carter v. Helmsley-Spear, Inc.*[134] and the fact that many of the issues faced in *Martin* were governed by agency and contract law.[135] Ultimately, the *Martin* court relied on the holding in *Chi-Boy Music v. Charlie Club, Inc.*[136] that attorney's fees may be awarded "'for reasons other than simply making the plaintiff whole, such as encouraging the assertion of colorable copyright claims and deterring infringement.'"[137] Recognizing that the statutory damages award "does not compensate Martin fully," that not awarding costs and fees "would have the effect of reducing further the adequacy of the damages award," and an award would "encourage artists . . . to assert their VARA rights in court," the court granted reasonable attorney's fees to Martin.[138] In this way, the court appears uniquely to have fashioned a quasi-damages remedy, on principles of equity and a policy of making legal action more available to copyright plaintiffs, based on a statutory provision for court costs and attorney's fees.

CONCLUSION

In sum, the year ending September 30, 1998 produced several published decisions that will affect the acquisition, protection and enforcement of intellectual property rights. Indiana law practitioners should be aware of these pronouncements as they counsel clients on these issues. The protection of trade secrets, the scope of potential patent protection, the use of the internet, and protection of artist's are just some of the matters the practitioner should consider as intellectual property plays an ever-greater role in the development and success of business.

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130. *Id.*
131. *Id.*
132. *Id.* at 812 (quoting 17 U.S.C. § 505 (1994)).
133. *Id.*
134. 861 F. Supp. 303 (S.D.N.Y. 1994), *aff'd*, 71 F.3d 77 (2d Cir. 1995).
135. *See Martin*, 4 F. Supp. 2d at 812.
136. 930 F.2d 1224 (7th Cir. 1991).
137. *Martin*, 4 F. Supp. 2d at 812 (quoting *Chi-Boy Music*, 930 F.2d at 1230).
138. *Id.*

RECENT DEVELOPMENTS IN THE INDIANA LAW OF PRODUCT LIABILITY

R. ROBERT STOMMEL*
DINA M. COX**

INTRODUCTION

During this survey period[1] the Indiana courts issued a number of significant product liability decisions. The courts discussed how to prove a product defect, clarified the distinction between a product and a service, applied the sophisticated user/bulk supplier doctrine, addressed the issue of when the statute of limitations begins to run, and defined additional parameters for the introduction of expert testimony under *Daubert*.[2]

I. PROVING PRODUCT DEFECT

In *Ford Motor Co. v. Reed*,[3] the Indiana Court of Appeals further defined the sufficiency of evidence necessary to prove the existence of a product defect. In that case, approximately six months after the Reeds purchased a new Ford Mustang, the car caught fire while parked in their garage.[4] When Murlin Reed opened the garage door, he found flames coming from inside of the Mustang. He opened the passenger door and put the fire out with a garden hose. After extinguishing the fire, he had difficulty breathing, his head hurt, his lungs hurt, and he was coughing.[5] He eventually required surgery to relieve his continuous headaches and blocked sinuses.[6] The Reeds brought an action against Ford Motor Company ("Ford") for strict liability, alleging a manufacturing defect in the electrical components within the Mustang's console.[7]

At trial, the court instructed the jury that the Reeds could prove the existence of a defect in one of four ways:

> 1. [p]laintiffs may produce an expert to offer direct evidence of a specific manufacturing defect;
> 2. plaintiffs may use an expert to circumstantially prove that a specific defect caused the product failure;
> 3. plaintiffs may introduce direct evidence from an eyewitness of the malfunction, supported by expert testimony explaining the

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* Attorney, Lewis & Wagner, Indianapolis. B.B.A., 1979, University of Wisconsin—Madison; J.D., *cum laude*, 1982, Indiana University School of Law—Indianapolis.

** Attorney, Lewis & Wagner, Indianapolis. B.G.S., *cum laude*, 1991, Ball State University; J.D., *cum laude*, 1995, Indiana University School of Law—Indianapolis.

1. October 1, 1997 to September 30, 1998.
2. Daubert v. Merrell Dow Pharm., Inc., 509 U.S. 579 (1993).
3. 689 N.E.2d 751 (Ind. Ct. App. 1997)
4. *Id.* at 752.
5. *See id.* at 753.
6. *See id.*
7. *See id.*

possible causes of the defective condition; and

4. plaintiffs may introduce inferential evidence by negating other possible causes.[8]

At both the end of the Reeds' case and again at the close of all evidence, Ford moved for a judgment on the evidence, claiming that there was insufficient evidence to prove a defect in the Mustang or to prove that Murlin Reed's injuries were proximately caused by the fire.[9] The trial court denied both motions and Ford appealed, arguing that "although there was testimony that the fire in question started in the Mustang's center console, no witness could pinpoint the identity of the specific defect."[10]

The court of appeals first noted that the trial court's jury instruction on proof of defect was taken from a decision that questioned whether Indiana recognized the doctrine of *res ipsa loquitur* for proof of a manufacturing defect.[11] Although pointing out that *res ipsa loquitur* is inappropriate in a product liability action under Indiana law,[12] the court nevertheless adopted the four methods of proof set forth in the jury instruction as "helpful tools" in determining whether there was sufficient evidence to prove the existence of a defect.[13]

Relying on *Bishop v. Firestone Tire & Rubber Co.*,[14] Ford argued that a defect in the Mustang was not necessarily proven simply because the product failed.[15] In *Bishop*, the plaintiff was injured when a lock ring assembly separated and ejected from a rim gutter while the plaintiff was repairing tires. Although Bishop's expert testified that the lock ring may separate if incorrectly assembled, there was no evidence that the lock ring actually contained a defect.[16] The court refused to allow an inference that the lock ring was defective merely because it separated and ejected from the rim while the plaintiff inflated the tire because such an inference would be based on undue speculation.[17] Similar to the plaintiff's expert in *Bishop*, the plaintiffs' expert in *Reed* admitted that he could not pinpoint the exact cause of the fire in the Mustang.[18]

Unlike the expert in *Bishop*, however, the Reeds' expert did opine that the specific cause of the fire was a failure of the electrical components within the console that are associated with the keypad for the mirrors and also identified a

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8. *Id.* at 753. This instruction was based on the test for proving the existence of a defect set forth in *Whitted v. General Motors Corp.*, 58 F.3d 1200, 1207 (7th Cir. 1995).

9. *See Reed*, 689 N.E.2d at 753.

10. *Id.*

11. *Id.* at 754.

12. *Id.* at 754 (citing SCM Corp. v. Letterer, 448 N.E.2d 686 (Ind. Ct. App. 1983)).

13. *Id.*

14. 814 F.2d 437 (7th Cir. 1987).

15. *See Reed*, 689 N.E.2d at 755.

16. *See Bishop*, 814 F.2d at 443.

17. *Id.*

18. *Reed*, 689 N.E.2d at 755.

wire taken from the console that evidenced electrical fault.[19] In addition, the Reeds "all but eliminate[d] every possibility but a defect in the console."[20] They had owned the car for only five months, and the fire occurred in an area of the car to which they did not have access.[21] "Absent some indication of an extraneous cause, the fact that there was a fire is also circumstantial evidence that there was a defect."[22] The court concluded that this, combined with the plaintiffs' expert's opinion that an electrical defect in the console caused the fire, was enough evidence for the jury to conclude that a defect in the console caused the fire.[23] The trial court's denial of Ford's motion for judgment on the evidence was therefore affirmed.[24]

Shortly after the Indiana Court of Appeals announced its decision in *Reed*, the United States Court of Appeals for the Seventh Circuit again addressed the issue of product defect in *Moss v. Crosman Corp.*[25] The court was faced with the question of whether under Indiana's Product Liability Law a BB gun may be considered defective and unreasonably dangerous because of its design or warnings.[26]

In *Moss*, Larry Moss bought his seven-year-old son, Josh, a Crosman 760 Pump Master BB Gun. On September 28, 1993, Josh was playing with the BB gun when his eleven-year-old cousin, Tim Arnett, came over. When it was Tim's turn to shoot, Josh hid behind a tree located fifteen feet in front of where Tim was standing. Tim pumped the gun three or four times and fired. At that instant, Josh poked his head out from behind the tree, was struck in the eye, and died almost immediately when the BB entered his brain.[27]

Josh's parents (the "Mosses") sued Crosman Corporation, the manufacturer of the gun, Coleman, a former owner of Crosman, and Kmart Corporation, the seller of the gun.[28] They claimed that "the defendants caused Josh's death by selling an air gun with a dangerous velocity and by failing to provide adequate warnings detailing the dangers associated with the gun."[29] The claim against Coleman was later dismissed by stipulation.[30] After preliminary discovery, the district court, applying Indiana law, granted the motion for summary judgment filed by Crosman and Kmart.[31] The Mosses appealed, but the Seventh Circuit

19. *See id.*
20. *Id.*
21. *See id.*
22. *Id.*
23. *Id.*
24. *See id.*
25. 136 F.3d 1169 (7th Cir. 1998).
26. *Id.* at 1171.
27. *See id.* at 1170-71.
28. *See id.* at 1171.
29. *Id.*
30. *See id.*
31. *See id.*

affirmed the district court's judgment.[32]

Although they couched their argument in design defect language, the Mosses claimed that the Pump Master had far more firepower than they or any other reasonable person would have expected.[33] The court noted that "this is not a claim that the air gun was failing to perform the functions for which it had been designed . . . [or] that some alternative design would have made a gun with the same firepower more safe."[34] Rather, "it is a complaint about the Moss lack of knowledge concerning this gun, and their failure to appreciate what kind of weapon they had purchased for their young son."[35] In short, the Moss' defective design argument boiled down to a failure to warn theory.[36] The Mosses were claiming that, had they known how far, or how fast, and with what penetrating power that the pellets shot from the Pump Master would go, they might have made a different decision.[37]

With respect to the failure to warn theory, the court addressed the issue of whether the Mosses were "entitled to reach the jury on a showing that the air gun was defective because of inadequate warnings alone, or if . . . there is an independent requirement under [Indiana] law to show that the product is unreasonably dangerous."[38] After observing that the answer to this question is unclear under Indiana law, the court held that "Indiana continues to require a showing of unreasonable danger as one element of the plaintiff's case."[39]

The court noted that Indiana "defines the term 'unreasonably dangerous' to refer to 'any situation in which the use of a product exposes the consumer to a risk of physical harm to an extent beyond that contemplated by the ordinary consumer . . . .'"[40] The Mosses argued that, even if the average person knows that BB guns "can cause flesh wounds, loss of eyes, etc.," that same person might be "specifically unaware that a BB gun would be as powerful as the Pump Master and thus could cause death."[41] However, the court stated that "the 760 Pump Master did not place users at risk of injuries *different in kind* from those an average consumer might anticipate."[42] The fact that the gun caused death rather than serious injury did "not transform the fundamental nature of the injury."[43] Thus, according to the court, the 760 Pump Master could not be regarded as unreasonably dangerous because the average person is aware of the danger that

32. *Id.*

33. *See id.* at 1173.

34. *Id.*

35. *Id.*

36. *See id.*

37. *See id.*

38. *Id.* at 1174.

39. *Id.*

40. *Id.* (quoting IND. CODE § 33-1-1.5-2(7) (Supp. 1997) (recodified at IND. CODE § 34-6-2-146 (1998)).

41. *Id.* at 1175.

42. *Id.* (emphasis added).

43. *Id.*

a projectile fired from a BB gun can hit a person and cause serious injury.[44] The court therefore affirmed summary judgment in favor of the defendants because the Mosses could not prove that the gun was unreasonably dangerous.[45]

Alternatively, the Seventh Circuit held that "the defendants would be able to establish the affirmative defense of incurred risk."[46] To gain the protection of this defense, "'it is not enough that a plaintiff merely have a general awareness of a potential for mishap.'"[47] Rather, the defense "'demands a subjective analysis focusing upon the plaintiff's actual knowledge and appreciation of the specific risk and a voluntary acceptance of that risk.'"[48] The court found the evidence "overwhelming that Larry Moss was fully aware that the 760 Pump Master could pierce the eye and flesh. He saw the warning about death and assumed that it meant the gun could kill birds and small animals."[49] Larry gave warnings to his son that spoke "eloquently about his knowledge of the risks the gun posed."[50] Consequently, "Larry [Moss] incurred the risk of the type of injury Josh suffered when [Larry] bought the gun."[51]

The United States Court of Appeals for the Seventh Circuit also discussed how to prove a product defect under Indiana law in *McMahon v. Bunn-O-Matic Corporation*.[50] In that case, Jack and Angelina McMahon were on a long-distance auto trip. They stopped at a Mobil station to buy a cup of coffee. Jack asked Angelina to remove the plastic lid while he drove. Angelina decided to pour some of the coffee into a small cup that would be easier for Jack to handle. In the process, the coffee flooded her lap, and Angelina suffered second and third degree burns causing pain and scars on her left thigh and lower abdomen.[51] The McMahons believed that the foam cup collapsed either because it was poorly made or because inordinately hot coffee weakened its structure. They sued the producers of the cup and lid and the manufacturer of the coffee maker.[52]

The McMahons' claims against the producers of the cup and lid were settled.[53] Their claims against the manufacturer of the coffee maker, Bunn-O-Matic, were summarily resolved by the district court in favor of Bunn-O-Matic.[54] The district court observed that both McMahons conceded during their depositions that "'hotness' was one of the elements they value in coffee and that

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44. *Id.*
45. *Id.*
46. *Id.* (citing IND. CODE 33-1-1.5-4(b)(1) (Supp. 1997) (recodified at IND. CODE § 34-20-6-3 (1998)).
47. *Id.* (quoting Clark v. Wiegand, 617 N.E.2d 916, 918 (Ind. 1983)).
48. *Id.* (quoting *Clark*, 617 N.E.2d at 918).
49. *Id.* at 1176.
50. *Id.*
51. *Id.*
50. 150 F.3d 651 (7th Cir. 1998)
51. *See id.* at 653.
52. *See id.*
53. *See id.*
54. *See id.*

they sought out hot coffee, knew it could burn, and took precautions as a result."[55] According to the district court, these concessions foreclosed the possibility of recovery.[56]

In its review of the district court's entry of summary judgment in favor of Bunn-O-Matic, the Seventh Circuit Court of Appeals first commented on the parties' litigation strategy.[57] The court noted that, while the McMahons proceeded on the assumption that Bunn-O-Matic made and sold coffee, Bunn-O-Matic actually sold and distributed a tool that retailers use to make coffee.[58] The court found Bunn-O-Matic's failure to challenge this perspective "puzzling."[59] The court asked:

> Why should a tool supplier be liable in tort for injury caused by a product made from that tool? If a restaurant fails to cook food properly and a guest comes down with food poisoning is the oven's manufacturer liable? Our concern is rooted not in the privity doctrine of by gone years but in the belief that tort doctrine must reflect the way in which different actors cooperate to improve safety. Consider the plaintiffs' claim that they should have received warnings. How is a manufacturer of coffee-making machines to deliver them? Many consumers of coffee never see the machine that made it—someone brings coffee to the customer in a cup or pot . . . .; a fast food outlet may deliver a sealed container to a take-out window . . . or place the coffee maker so far behind the counter that customers cannot read whatever warnings it bears. And coffee makers are small; where would a warning more elaborate than "Hot!" go? If warnings are in order, then, they belong on a restaurant's menu, or on the cups containing take-out coffee.[60]

Nevertheless, because both sides treated Bunn-O-Matic and the retailer of the coffee identically, the court of appeals proceeded on that basis "while doubting that it is sound."[61]

The McMahons first claimed that Bunn-O-Matic failed to warn consumers about the severity of burns that hot coffee can produce.[62] Yet, the McMahons already knew that coffee is served hot and that it can cause burns and, according to the court, did not need to be reminded.[63] Furthermore, the court observed:

> What would this warning have entailed? . . . [T]hat this coffee was unusually hot and therefore capable of causing severe burns? Warning

55. *Id.* at 654.
56. *See id.*
57. *Id.*
58. *Id.*
59. *Id.*
60. *Id.* at 654-55.
61. *Id.* at 655.
62. *See id.*
63. *Id.*

> consumers about a surprising feature that is potentially dangerous yet hard to observe could be useful, but the record lacks any evidence that 179 [degrees Fahrenheit] is unusually hot for coffee. Neither side submitted evidence about the range of temperatures used by commercial coffee makers, or even about the range of temperatures for Bunn's line of products. The McMahons essentially ask us to take judicial notice that 179 [degrees Fahrenheit] is abnormal, but this is not the sort of incontestable fact for which proof is unnecessary.[64]

The court also noted other judicial opinions reporting an industry standard serving temperature between 175 and 185 degrees Fahrenheit and noted that "most consumers prepare and consume hotter beverages at home."[65] Finally, the court referenced the American National Standards Institute's ("ANSI's") standard for home coffee makers which allowed for the brewing and holding of coffee at a temperature not falling below 170 degrees Fahrenheit.[66] Accordingly, the court concluded that "coffee served at 180 [degrees Fahrenheit] by a roadside vendor, which doubtless expects that it will cool during the longer interval before consumption, does not seem so abnormal as to require a heads-up warning."[67]

Nonetheless, "[t]he McMahons insist[ed] that, although they knew that coffee can burn, they thought that the sort of burn involved would be a blister . . ., not a third degree burn."[68] In rejecting this claim, the court reasoned that Bunn-O-Matic could not be expected to deliver a medical education with each cup of coffee.[69] The court went on to note that insistence on more detail can make "any warning, however elaborate, seem inadequate."[70]

> Extended warnings present several difficulties, first among them that, the more text must be squeezed onto the product, the smaller the type and the less likely is the consumer to read or remember any of it. Only pithy and bold warnings can be effective. Long passages in capital letters are next to illegible, and long passages in lower case letters are treated as boilerplate. Plaintiff wants a warning in such detail that a magnifying glass would be necessary to read it. Many consumers cannot follow simple instructions (including pictures) describing how to program their video cassette recorders.[71]

The court noted that "Indiana has the same general understanding."[72]

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64. *Id.*
65. *Id.*
66. *Id.*
67. *Id.* at 656.
68. *Id.*
69. *Id.*
70. *Id.*
71. *Id.* (quoting Todd v. Societe 131C, S.A., 9 F.3d 1216, 1218-19 (7th Cir. 1993) (en banc) (applying Illinois law)).
72. *Id.*

The court further remarked that "Indiana does not require vendors to give warnings in the detail plaintiffs contemplate."[73] Instead, "[i]t expects consumers to educate themselves about the hazards of daily life—of matches, knives, and kitchen ranges, of bones in fish, and of hot beverages—by general reading and experience, knowledge they can acquire before they enter a mini mart to buy coffee for a journey."[74]

The McMahons next contended that any coffee served at more than 140 degrees Fahrenheit is unfit for human consumption and therefore a defective product because of its power to cause burns more severe than consumers expect.[75] The court noted that, in design defect cases, the plaintiff must establish that the manufacturer or seller failed to exercise reasonable care under the circumstances in designing the product.[76] In other words, a design defect claim in Indiana is based on negligence principles, "subject to the understanding that negligence means failure to take precautions that are less expensive than the net costs of accidents."[77] Moreover, the plaintiff must show "not only that the design is defective but also that the defective product is 'unreasonably dangerous.'"[78] In Indiana,

> "unreasonably dangerous" refers to any situation in which the use of the product exposes the user or consumer to a risk of physical harm to an extent beyond that contemplated by the ordinary consumer who purchases it, with the ordinary knowledge about the product's characteristics common to the community of consumers.[79]

The McMahons argued that, although they knew coffee could burn, Bunn-O-Matic's coffee "exposed them to harm extending beyond that contemplated by the ordinary consumer."[80] The court referred to several Indiana cases having rejected claims that a "consumer's failure to appreciate the gravity of the damage a product could do made it 'unreasonably dangerous,' [especially] when the consumers understood that the product could cause a serious injury."[81] Nonetheless, the court did not decide whether a third degree burn is a harm not contemplated by the ordinary consumer because, even if hot coffee may be considered unreasonably dangerous, the record was devoid of evidence showing that the coffee maker was defectively designed.[82]

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73. *Id.*
74. *Id.* at 656-57.
75. *See id.* at 654.
76. *Id.* at 657.
77. *Id.* (citations omitted).
78. *Id.*
79. *Id.* (quoting IND. CODE § 31-1.5-2(7) (Supp. 1997) (recodified at IND. CODE § 34-6-2-146 (1998)).
80. *Id.*
81. *Id.* (citing Moss v. Crosman Corp., 136 F.3d 1169, 1173-74 (7th Cir. 1998); Anderson v. P.A. Radosy & Sons, Inc., 67 F.3d 619, 624-26 (7th Cir. 1995)).
82. *Id.*

The McMahons attempted to show that the coffee maker was defectively designed by the testimony of Professor Diller.[83] Professor Diller opined that "at the temperatures at which this coffee was brewed and maintained the structural integrity of the foam cup into which the coffee was poured would be compromised making it more flexible and likely to give way or collapse when its rigged lid is removed."[84] Not only did the court disagree with laying this purported effect "at the door of Bunn rather than the cup's producer . . . or the retailer," the court further noted that Professor Diller offered nothing more than a bare conclusion.[85] He did not explain or empirically support his conclusion.[86] He did not explain how hot beverages could make foam cups too flexible, how much more flexible and under what circumstances, how likely to collapse the cups became, and how the failure rate of the cups varied with temperature.[87] According to the court, "'[a]n expert who supplies nothing but a bottom line supplies nothing of value to the judicial process.'"[88] Accordingly, Diller's affidavit was found to be inadmissible under *Daubert*.[89] Without Diller's affidavit, the McMahons had no evidence to support their theory of a design defect.[90]

Alternatively, the McMahons argued that the coffee should not have been served at more than 135 to 140 degrees Fahrenheit.[91] In a well-written, common sense passage, the court responded:

> [P]eople spend money to increase their risks all the time—they pay steep prices for ski vacations; they go to baseball games where flying bats and balls abound; they buy BB guns for their children knowing that the pellets can maim. They do these things because they perceive benefits from skiing, baseball, and target practice . . . . Indiana does not condemn products as defective just because they are designed to do things that create serious hazards. . . . To determine whether a coffee maker is defective because it holds the beverage at 179 [degrees Fahrenheit], we must understand the benefits of hot coffee in relation to its costs. As for costs, the record is silent. We do not know whether severe burns from coffee are frequent or rare. On the other side of the ledger, there are benefits for all coffee drinkers. Jack McMahon testified that he liked his coffee hot. Why did the [ANSI] set 170 [degrees Fahrenheit] as the minimum temperature at which coffee should be ready to serve? Diller

83. *See id.*

84. *Id.*

85. *Id.*

86. *See id.* at 658.

87. *See id.* at 657.

88. *Id.* at 658 (quoting Mid-State Fertilizer Co. v. Exchange Nat'l Bank, 877 F.2d 1333, 1339 (7th Cir. 1989)).

89. *See id.* (citing Daubert v. Merrell Dow Pharm., Inc., 509 U.S. 579 (1993)).

90. *See id.*

91. *See id.*

> does not make any effort to reconcile his "maximum 140 [degrees Fahrenheit]" position with the ANSI's "minimum 170 [degrees Fahrenheit]" position—though this is something that an engineer would be sure to do in scholarly work. Without some way to compare the benefits of a design change (fewer and less severe burns) against the costs (less pleasure received from drinking coffee), it is impossible to say that designing a coffee maker to hold coffee at 179 [degrees Fahrenheit] bespeaks negligent inattention to the risks.[92]

The court refused to consider it obvious that consumers derive no benefit from coffee served at temperatures hotter than 140 degrees Fahrenheit.[93] While the court found it easy to sympathize with Angelina McMahon, it noted that using the legal system to shift the costs of her injuries to someone else would have bad consequences for coffee connoisseurs who like their coffee hot.[94] "First-party health and accident insurance deals with injuries of the kind Angelina suffered without the high costs of adjudication, and without potential side effects such as luke warm coffee."[95]

II. PRODUCT VS. SERVICE

In *Whitaker v. T.J. Snow Co.*,[96] the Seventh Circuit Court of Appeals addressed whether the refurbishing of equipment constituted the provision of a service instead of the manufacturing of a product. The plaintiff in *Whitaker* was injured when her hand was caught in the pinch point of a seam welder as the welder reactivated in the middle of a weld cycle.[97] The plaintiff's employer, Walker, hired T.J. Snow Company ("Snow") to upgrade the electrical circuits of the seam welder. Snow added a new programming unit, several new circuits, and a new weld control; designed and built a water catch basin; and, cleaned and painted the machine. The shop order specifically prohibited Snow from rebuilding the basic welder.[98] Snow neither designed any of the new component parts, nor changed the welder's mechanical function. The parties agreed that the work Snow performed extended the useful life of the machine.[99] Snow was supposed to inspect the seam welder to determine if any guarding was necessary for pinch points, and, if so, to either furnish the required guards or tell Walker they were needed. Snow nevertheless failed to install any guards, to warn Walker, or to place warning stickers on exposed pinch points.[100]

In the trial court, the plaintiff waived her negligence claim and pleaded only

92. *Id.*
93. *Id.* at 658-59.
94. *Id.* at 659.
95. *Id.*
96. 151 F.3d 661 (7th Cir. 1998).
97. *See id.* at 663.
98. *See id.* at 662.
99. *See id.*
100. *See id.* at 663.

a warranty theory.[101] The plaintiff did not argue, however, that Snow installed any defective parts or that its work was otherwise unsatisfactory. Her only theory was that, given the extent of work performed by Snow on the machine, Snow was transformed into a manufacturer of the machine and was therefore liable for failing to ensure that parts of the machine unrelated to the work it performed had the proper guards and warnings.[102] The federal district court granted Snow's motion for summary judgment.[103] The district court found that Snow had neither sold, leased, nor otherwise placed the welder into the stream of commerce when it refurbished the machine for Walker.[104] The district court also found that the work Snow had performed was predominantly a service rather than a manufacture of a product and therefore fell outside the scope of the Indiana Product Liability Act.[105] On appeal, Whitaker limited her arguments to Snow's strict liability claim and focused on the product/service issue.

The Seventh Circuit first noted that the Indiana Product Liability Act, by its terms, does not apply to transactions which "'involve[ ] wholly or predominantly the sale of a service rather than a product.'"[106] This particular transaction was not "wholly" the sale of a service because Snow procured and installed component parts in the welder.[107] Thus, the issue was whether the transaction was "predominantly" for the sale of a service.[108]

After reviewing prior Indiana appellate and Seventh Circuit decisions in which the product/service distinction was addressed, the court in *Whitaker* determined that the critical question was whether the "predominant thrust" of the contract was for the sale of goods or for the rendering of services.[109] "The key distinction is between the repair or improvement of an existing machine, and the construction or rebuilding of a new machine."[110] Whether the work adds useful life to the equipment is not determinative because even routine maintenance adds to useful life.[111] Although the court conceded that the refurbishing work here went beyond routine maintenance, Snow's work focused on replacement of certain component parts specified by Walker and making sure that the machine

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101. *See id.*

102. *See id.* at 666.

103. Although Whitaker's amended complaint alleged only a warranty claim, Snow's motion for summary judgment briefed both the warranty issue and a claim for strict liability under the Indiana Product Liability Act. Because both parties addressed the strict liability issue in their summary judgment briefs, the Seventh Circuit found that the complaint had been constructively amended to include the strict liability claim. *Id.* at 663.

104. *See id.* at 662.

105. *See id.* at 664.

106. *Id.* (quoting IND. CODE § 33-1-1.5-2(6) (Supp. 1997) (modification in original) (recodified at IND. CODE § 34-6-2-114 (1998)).

107. *See id.*

108. *See id.*

109. *Id.*

110. *See id.* at 665-66.

111. *Id.* at 666.

was working properly. This was more like "custom work" than the manufacture of either the full seam welder or component parts for the machine.[112] The appellate court thus affirmed the summary judgment in Snow's favor.

III. SOPHISTICATED USER/BULK SUPPLIER DOCTRINE

In *Downs v. Panhandle Eastern Pipeline Co.*,[113] the Indiana Court of Appeals applied the "bulk supplier" doctrine to the supplier and transporter of natural gas.[114] In *Downs*, a local municipal gas utility purchased natural gas from Vesta. The gas was produced by Vesta from gas fields in Kansas and transported to the local gas utility through a pipeline system operated by Panhandle. The natural gas was produced and transported without an odorant. The local gas utility added an odorant after receiving the gas into its own system.[115] The local gas utility's distribution lines were over fifty years old and included home service lines made of bare steel pipe. Natural gas from a corroded steel service line seeped into the Downs' house where it was ignited by a wood burning stove. The Downs family was seriously injured by the explosion. Downs brought an action against numerous defendants, including Vesta and Panhandle.[116] Among many theories asserted against Vesta and Panhandle, Downs included claims for negligent failure to warn under the Restatement (Second) of Torts section 388[117] and for strict liability failure to warn under the Product Liability Act.[118] The trial court

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112. *See id.*

113. 694 N.E.2d 1198 (Ind. Ct. App. 1998).

114. This is the second time this case has reached the Indiana Court of Appeals on similar issues. *See* Natural Gas Odorizing, Inc. v. Downs, 685 N.E.2d 155 (Ind. Ct. App. 1997), *reviewed in*, R. Robert Stommel & Dina M. Cox, *Recent Developments in the Indiana Law of Product Liability*, 31 IND. L. REV. 707, 715 (1998).

115. *See Downs*, 694 N.E.2d at 1200.

116. *See id.* at 1201.

117. Section 388 of the Restatement (Second) of Torts provides:

> One who supplies directly or through a third person a chattel for another to use is subject to liability to those whom the supplier should expect to use the chattel with the consent of the other or to be endangered by its probable use, for physical harm caused by the use of the chattel in the manner for which and by a person for whose use it is supplied, if the supplier
>
> (a) knows or has reason to know that the chattel is or is likely to be dangerous for the use for which it is supplied, and
>
> (b) has no reason to believe that those for whose use the chattel is supplied will realize its dangerous condition, and
>
> (c) fails to exercise reasonable care to inform them of its dangerous condition or of the facts which make it likely to be dangerous.

RESTATEMENT (SECOND) OF TORTS § 388 (1965).

118. *See Downs*, 694 N.E.2d at 1201. Indiana's Product Liability Act states, in relevant part, that a product is defective if the seller fails to:

> (1) properly package or label the product to give reasonable warnings of danger

granted summary judgment to Vesta and Panhandle on both theories, and Downs appealed.[119]

In its analysis of the Downs' Restatement (Second) of Torts section 388 claim, the *Downs* court first noted that section 388 imposes on a supplier of dangerous goods a duty to inform the consumer of the facts that make the goods dangerous.[120] Because Panhandle was only the transporter and not the "supplier" of the natural gas, this theory did not apply to Panhandle.[121] Vesta was therefore the only defendant subject to potential liability under section 388.[122] The court then analyzed the section 388 claims against Vesta by applying the "bulk supplier" doctrine.[123]

Relying on a decision by the Supreme Court of Kansas,[124] the court held that a bulk supplier of natural gas has no duty to warn the ultimate consumer if the distributor of the gas has adequate knowledge of the dangers associated with the gas it purchases from the bulk supplier.[125] The bulk supplier's duty to warn the distributor is satisfied when the distributor knows of the dangerous characteristics of the gas and safe methods for handling it, and the distributor has operated a business distributing it for many years.[126] Here, the local gas utility "was well aware of the dangers associated with transporting natural gas and . . . of the potential problems with its own distribution system."[127] The local utility had developed programs to detect and repair leaks and corrosion. An employee of the utility admitted the potential safety problems that could arise with the use of bare steel pipes to distribute the gas. The utility even undertook to warn its own customers of the dangers of gas. The evidence presented on summary judgment thus failed to show, under section 388(b), that the local gas utility was not fully aware of the dangers associated with distributing gas generally or through its own pipelines.[128] Because the local gas utility was adequately warned of the dangers, Vesta, as a bulk supplier, had no duty to directly warn the Downses.[129]

The appellate court next addressed Downs' theory of strict liability for

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about the product; or

(2) give reasonably complete instructions on the proper use of the product; when the seller, by exercising reasonable diligence, could have made such warnings or instructions available to the user or consumer.

IND. CODE § 34-20-4-1 (1998) (formerly IND. CODE § 33-1-1.5-2.5 (1993)).

119. *See Downs*, 694 N.E.2d at 1200.

120. *Id.* at 1207.

121. *See id.*

122. *See id.* at 1207-08.

123. *Id.* at 1208.

124. *Id.* (citing Jones v. Hittle Serv., Inc., 549 P.2d 1383 (Kan. 1976)).

125. *Id.* at 1208.

126. *See id.* (citing Parkinson v. California Co., 255 F.2d 265, 268 (10th Cir. 1958)).

127. *Id.* at 1209.

128. *See id.*

129. *See id.*

failure to warn under the Product Liability Act.[130] Under this theory, the Downs did not argue that Panhandle and Vesta were strictly liable for failing to provide warnings to them directly, but only that Panhandle and Vesta were strictly liable for failure to provide warnings to the local gas utility.[131] Specifically, the Downs contended that the defendants had a duty to warn the local gas utility about using bare steel lines and about using the proper amount of odorant to ensure that their unodorized product would be safer.[132] The court rejected this argument for two reasons.[133] First, as a condition for liability under the Product Liability Act, the product must reach the user or consumer without substantial alteration in the condition in which it is sold.[134] There was no question here that the unodorized gas supplied by Vesta and transported by Panhandle was expected to be substantially altered by the local gas utility's addition of its own odorant.[135] Second, the "bulk supplier" doctrine under section 388 applied equally to the Downs' strict liability failure to warn claims.[136] The Product Liability Act states that where an action is based on failure to warn, the plaintiff must prove that the manufacturer or seller failed to exercise reasonable care under the circumstances in providing the warnings.[137] Under both the Product Liability Act and the Restatement section 388, the supplier of natural gas has no duty to warn the gas distributor if the distributor already has adequate knowledge of the dangers associated with the gas.[138] Because there was no information about natural gas or the handling of gas that could have been provided by Panhandle and Vesta that would have improved the local gas utility's knowledge, Panhandle and Vesta did not fail "to exercise reasonable care under the circumstances" by not providing warnings to the local utility.[139]

In another case addressing the sophisticated user/bulk supplier doctrine, *Taylor v. Monsanto Co.*,[140] the Seventh Circuit Court of Appeals affirmed the federal district court's grant of summary judgment based on the sophisticated user doctrine.[141] The plaintiffs in *Taylor* sued Monsanto, the manufacturer of polychlorinated biphenyls ("PCBs"), for injuries they claimed were the result of

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130. *Id.* at 1210.

131. *See id.* at 1211.

132. *See id.*

133. *Id.* at 1211-12.

134. *See id.* at 1211 (citing IND. CODE § 33-1-1.5-3(a) (Supp. 1997) (recodified at IND. CODE § 34-20-2-1 (1998)).

135. *See id.*

136. *See id.* at 1212.

137. *See id.* (citing IND. CODE § 33-1-1.5-3(b) (Supp. 1997) (recodified at IND. CODE § 34-20-4-1 (1998)).

138. *See id.*

139. *Id.* (quoting IND. CODE § 33-1.1.5-3(b) (Supp. 1997) (recodified at IND. CODE § 34-20-4-2 (1998)).

140. 150 F.3d 806 (7th Cir. 1998).

141. *Id.* at 807. The federal district court opinion is reported in *Baker v. Monsanto Co.*, 962 F. Supp. 1143 (S.D. Ind. 1997), *reviewed in* Stommel & Cox, *supra* note 114, at 715.

workplace exposure to PCBs while employed by Westinghouse Electric Company ("Westinghouse").[142] The Seventh Circuit first noted that Indiana courts have clearly recognized the "sophisticated intermediary" defense, which holds that the manufacturer has no duty to warn the ultimate user when the product is sold to a "knowledgeable or sophisticated intermediary" whom the manufacturer has adequately warned. In order for this doctrine to apply, the intermediary "must have knowledge or sophistication equal to that of the manufacturer, and the manufacturer must be able to rely reasonably on the intermediary to warn the ultimate consumer."[143] The court then noted that the issue framed on appeal presented no questions of law, only factual issues regarding whether Westinghouse was a sophisticated intermediary to whom Monsanto had given adequate warnings about PCBs.[144]

In determining whether Westinghouse was a "sophisticated intermediary," the court reviewed the "uncontroverted evidence that Westinghouse was highly sophisticated about PCBs."[145] Westinghouse gave Monsanto its own specifications for the PCB fluids to be produced, which were delivered by Monsanto in large quantities by railroad car, tank truck, and fifty-five-gallon drums. Westinghouse had used PCBs for over forty years, had developed vast in-house medical, engineering, and environmental expertise about PCBs, and had prepared its own Material Safety Data Sheets for PCB-laden fluids. Westinghouse's knowledge of PCBs was so sophisticated that it participated in federal and industry task forces and working committees on PCBs.[146]

In an attempt to overcome this evidence, the plaintiffs argued that, although Westinghouse may have been expert about environmental matters related to PCBs, it was unsophisticated about the human health hazards associated with PCBs.[147] The court rejected this argument on two grounds.[148] First, the court rejected the plaintiffs' attempt to "fine-tune" the sophisticated intermediary doctrine to require Westinghouse to have specific expertise on human health issues related to PCBs.[149] The more appropriate view of the level of sophistication required to meet the doctrine is a "broad, multi-factor view."[150] Applying this view, the court took into consideration the plaintiffs' allegation in their complaint that Westinghouse knew of the medical risks of PCBs.[151] Second, the court noted that the record was void of any evidence that Westinghouse was ignorant or unsophisticated about the health effects of PCBs.[152] Instead, the

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142. *Taylor*, 150 F.3d at 807.
143. *Id.* at 808.
144. *Id.*
145. *Id.*
146. *See id.*
147. *See id.*
148. *Id.* at 808-09.
149. *Id.* at 808.
150. *Id.* at 809.
151. *Id.*
152. *Id.*

plaintiffs had relied on "conclusory and self-serving allegations unsupported by the record."[153]

The Seventh Circuit next addressed the second prong of the sophisticated intermediary defense: Whether Monsanto had adequately warned Westinghouse about PCBs.[154] The plaintiffs argued that, even if Westinghouse were a sophisticated intermediary, Monsanto nevertheless failed to warn Westinghouse about PCB dangers because the health hazard advisories which Monsanto supplied to Westinghouse were "warnings with a wink" based on misrepresentations Monsanto allegedly made regarding PCB safety.[155] The plaintiffs relied heavily on a statement in a publication by the American National Standards Institute ("ANSI") that PCB exposure caused only limited adverse health effects.[156] Monsanto had provided a copy of the ANSI publication to Westinghouse. The court, however, refused to impute the publication to Monsanto, stating: "ANSI is not Monsanto, and the statements of the former cannot be reasonably imputed to the latter."[157] Although a Monsanto employee chaired the ANSI committee and Monsanto was the sole domestic manufacturer of PCBs, the Seventh Circuit found that "it simply pushes the matter too far to impute the ANSI committee's statement to Monsanto" and "[n]o reasonable jury could find otherwise."[158] The court also noted correspondence from Monsanto to Westinghouse's Personnel Department in which Monsanto warned at length about the risk of skin irritation, chloracne, injury to cellular tissue, serious liver injury, and even death from PCB exposure.[159] Because the letter described PCBs as potentially dangerous substances that should be properly handled in a safe manner, it would be unreasonable as a matter of law for a jury to interpret the letter otherwise.[160]

Having satisfied itself that Westinghouse was sophisticated about PCBs and that Monsanto warned Westinghouse about the dangers of PCBs with more than a "wink," the Seventh Circuit held that the "sophisticated intermediary doctrine" applied and affirmed the district court's grant of summary judgment in favor of Monsanto.[161]

IV. Statute of Limitations

During this survey period, the Indiana Court of Appeals once again addressed the issue of when the statute of limitations begins to run in a chemical exposure

153. *Id.*
154. *Id.*
155. *See id.*
156. *See id.*
157. *Id.* at 809-10.
158. *Id.* at 810.
159. *Id.*
160. *See id.*
161. *Id.*

product liability case. In *Degussa Corp. v. Mullens*,[162] the plaintiff worked for an animal feed company where she mixed powdered and liquid ingredients into livestock feeds.[163] She claimed to suffer permanent lung damage due to her exposure to the ingredients that were manufactured by the defendants.[164] The defendants moved for summary judgment based on the two-year statute of limitations contained in the Product Liability Act.[165] The trial court denied their motion, and the defendants obtained an interlocutory appeal.[166]

On appeal, the plaintiff argued that there was no evidence that any doctor had determined, more than two years before she filed her complaint, the likely or probable cause of her medical condition and that her condition was likely or probably caused by her chemical exposure at work.[167] Based on its review of prior Indiana and Seventh Circuit opinions interpreting when a cause of action "accrues" under the two-year statute of limitations, the court in *Mullens* rejected the plaintiff's suggested standard.[168] After noting that the "discovery rule provides a two-year period during which a potential plaintiff has a fair opportunity to investigate,"[169] the court stated: "The discovery rule does not toll the statute of limitations until all uncertainty is eliminated . . . . Rather, once a plaintiff confirms or is informed that a product is a possible cause of her illness, the fair opportunity to investigate for up to two years commences."[170] Thus, the question on appeal was "whether there [was] a genuine issue of material fact with respect to when Mullens had a fair opportunity to investigate the cause of the injury, rather than when she knew the likely or probable cause of the injury."[171]

In February 1992, Mullens went to the emergency room with respiratory problems that began at work. She told the emergency room physician that she worked with chemicals.[172] When her respiratory problems worsened approximately one month later, she visited her family physician and took with her a label from one of the chemicals. Mullens told her family physician that she was exposed to chemicals at work and showed him the label. Her family physician testified that Mullens told him that she thought her exposure to dust at

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162. 695 N.E.2d 172 (Ind. Ct. App. 1998).

163. *Id.* at 173.

164. *See id.* at 173-74.

165. *See id.* at 174. The Product Liability Act provides, in part, that "a product liability action must be commenced: (1) within two (2) years after the cause of action accrues; . . . ." IND. CODE § 34-20-3-1 (1998) (formerly IND. CODE § 33-1-1.5-5 (Supp. 1997)).

166. *See Mullens*, 695 N.E.2d at 174.

167. *See id.* at 176.

168. *Id.*

169. *Id.* The "discovery rule" for accrual of claims arising out of illness caused by prolonged toxic exposure provides that the statute of limitations begins to "run from the date the plaintiff knew or should have discovered that [she] suffered an injury or impingement, and that it was caused by the product or act of another." Barnes v. A.H. Robins Co., 476 N.E.2d 84, 87-88 (Ind. 1985).

170. *Mullens*, 695 N.E.2d at 176 (citations omitted).

171. *Id.*

172. *See id.*

work was contributing to her illness.[173] Although his ultimate diagnosis was unclear at the time, the family physician told Mullens that there was a "possibility" that her medical condition was work related.[174] He also told her that she needed to further investigate the connection between her illness and her work exposure.[175] Mullens acknowledged this conversation.[176] On March 18, 1992, Mullens filled out a worker's compensation form because she suspected that her respiratory problems were caused by workplace exposures. Mullens filed her lawsuit on March 25, 1994.[177]

In an attempt to overcome these facts, Mullens submitted her own affidavit in opposition to the defendants' motion for summary judgment, in which she claimed that she was confused and that she did not know with certainty the source of her problems until March of 1994.[178] Based on the plaintiff's own knowledge and the information provided to her by her physicians, the court determined that Mullens had a fair opportunity to investigate her injury more than two years before she filed her complaint.[179] The court determined that Mullens had a medical condition sufficient to be considered an injury at least by February and March of 1992 and that the evidence relating to her worker's compensation claim and the visits to her family physician clearly established that she suspected her work exposure was a possible cause of her illness.[180] Her suspicions were confirmed by her doctor's statement that the chemicals were a possible cause of her illness.[181] "As such, because Mullens was told that the chemicals were a possible cause of her illness, the fair opportunity to investigate for up to two years commenced at least at that point."[182]

The appellate court also rejected the plaintiff's attempt to create an issue of fact through her own affidavit, stating that "a lack of confusion on a potential plaintiff's part is not the test of when the statute of limitations begins to run."[183] Instead, "the statute begins to run when suspicion arises, not when all confusion or doubt is dissipated."[184] In addition, under the discovery rule, the test for what the plaintiff knew or should have discovered is an objective standard—what a reasonable person should have known, not what the plaintiff actually knew.[185] Here, the uncontradicted evidence that plaintiff took the chemical label to her doctor and that he told her that her condition may be related to her work exposure

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173. *See id.*
174. *See id.* at 177.
175. *See id.*
176. *See id.*
177. *See id.*
178. *See id.* at 178.
179. *Id.*
180. *Id.* at 177.
181. *See id.*
182. *Id.* at 178.
183. *Id.*
184. *Id.*
185. *See id.*

was "sufficient to establish that Mullens had a fair opportunity to investigate her injury and its cause at that time."[186] The appellate court, therefore, reversed the trial court's denial of summary judgment and remanded with instructions to enter judgment in favor of the defendants.[187]

V. Expert Opinion Testimony

In 1996, the Indiana Court of Appeals specifically adopted the standards set forth in *Daubert v. Merrell Dow Pharmaceuticals, Inc.*[188] for determining the admissibility of expert scientific testimony under Indiana Rule of Evidence 702.[189] During this survey period, additional guidance for assessing the admissibility of such evidence was offered by the Seventh Circuit Court of Appeals in *Ancho v. Pentek Corp.*[190]

In *Ancho,* the plaintiff was employed as a process manager at a corrugated cardboard production facility. A Pentek Intelligent Automatic Car ("PIAC") materials handling system, manufactured by Pentek, was in use at the plant. The PIAC consisted of five fixed roller conveyers and an automatic transfer car.[191] The transfer car moved along a rail running north-south set below the floor of the plant, while the top of the car was elevated above the floor. The transfer car was used to carry loads of corrugated board between the roller conveyors at the plant. As the transfer car moved between the various conveyors at the plant, it passed through a number of "pinch points" that could be hazardous to employees due to the transfer car's tendency to catch, pull, pinch, and crush hands, arms, fingers, and feet that became entangled in the car.[192]

The transfer car operated at speeds ranging from .45 miles-per-hour to three-miles-per hour. When the car was in motion, a warning system activated a loud horn as well as flashing lights to warn workers to stay clear of the track. Numerous signs and red stickers were in placed on and about the roller conveyer and transfer car, warning of the risk of hazardous machinery and "pinch points."[193] The plant's floor across which the car operated was marked with yellow lines and red paint. Moreover, electronic sensors attached to the transfer car automatically caused the car to shut down whenever an object was detected traversing the path of the moving car.[194]

On October 4, 1993, the plaintiff was inspecting some corrugated board at

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186. *Id.*

187. *Id.*

188. 509 U.S. 579 (1993).

189. *See* Hottinger v. TruGreen Corp., 665 N.E.2d 593 (Ind. Ct. App. 1996), *reviewed in* R. Robert Stommel & Dina M. Cox, *Recent Developments in the Indiana Law of Products Liability*, 30 Ind. L. Rev. 1227, 1241 (1997).

190. 157 F.3d 512 (7th Cir. 1998).

191. *See id.*

192. *See id.*

193. *See id.* at 513-14.

194. *See id.* at 514.

one of the roller conveyor locations. While performing the inspection, he moved to the other side of the conveyor and proceeded to walk around the end of the conveyor, requiring him to cross the transfer car rail.[195] He crossed the transfer car's travel aisle without paying attention to the fact that the car was traveling down the rail towards him. His left foot became locked in a "pinch point," and he sustained serious permanent damage.[196]

Plaintiff's expert, Ronald Lobodzinski, submitted a written report prior to trial opining that Pentek's design of the PIAC failed to eliminate the unreasonably dangerous pinch points and failed to provide adequate safety devices to protect persons from the pinch points.[197] He proposed that: (1) the movable transfer car be eliminated from the materials handling system, or (2) safety devices near the pinch points be installed, such as electronic safety devices or mats, which would sense when someone was near the pinch point and thereby stop the transfer car.[198]

Pentek deposed Lobodzinski regarding his qualifications and investigation.[199] Pentek then moved in limine to bar Lobodzinski from testifying at trial, arguing that Lobodzinski did not qualify as an expert pursuant to *Daubert*.[200] The trial court granted Pentek's motion and subsequently entered summary judgment in Pentek's favor.[201] Plaintiff appealed to the United States Court of Appeals for the Seventh Circuit.[202] Plaintiff argued on appeal that the trial court failed to correctly articulate and apply the *Daubert* standard in barring Lobodzinski's testimony.[203]

The appellate court reiterated that Federal Rule of Evidence 702 ("Rule 702") and *Daubert* require a two-step inquiry when evaluating the admissibility of expert testimony.[204] First, the testimony must be reliable—it must have been "subjected to the scientific method" and rise above "subjective belief or unsupported speculation."[205] Second, the testimony must be relevant—it must "assist the trier of fact in understanding the evidence or in determining a fact in issue."[206] Moreover,

> [f]our non-exclusive "guideposts" are pertinent in assessing the reliability and validity of the expert's scientific methodology: "(1) whether [the expert's theory] can and has been tested; (2) whether [his

195. *See id.*
196. *See id.*
197. *See id.* at 514.
198. *See id.*
199. *See id.*
200. *See id.*
201. *See id.* at 514-15.
202. *See id.* at 515.
203. *See id.*
204. *Id.*
205. *Id.*
206. *Id.*

> theory] has been subjected to peer review and publication; (3) the known or potential rate of error; and (4) the general acceptance of the theory."[207]

Furthermore, the court noted that the *Daubert* court did not presume to set out a "'definitive checklist or test.'"[208] Rather, the district court judge's inquiry was intended to be "'flexible.'"[209]

The court of appeals noted that Lobodzinski had no expertise in plant design and had not observed the transfer car in operation, "much less even take the time to visit the accident site."[210] While the district court judge did not specifically mention the four guideposts of *Daubert* in his oral ruling, the court concluded that the judge's decision, when "read in totality," demonstrates that the judge relied upon the *Daubert* standard when issuing his ruling.[211] The court further held:

> [W]e all understand that oral rulings are not as formalistic, definitive, and specific as written ones. Trial judges need only follow (i.e., adhere to) *Daubert* when making a Rule 702 determination, . . . they are not required to recite the *Daubert* standard as though it were some magical incantation.[212]

In upholding the trial court, the Seventh Circuit reaffirmed the rule that an expert's qualifications may very well bear upon the scientific validity of the expert's testimony.[213] The court concluded that Lobodzinski, a mechanical engineer, did not possess the requisite qualifications to render an opinion as to the feasibility of installing a fixed-conveyor materials handling system or other plant reconfiguration alternatives.[214]

In *Lytle v. Ford Motor Co.*,[215] the Indiana Court of Appeals likewise addressed the application of *Daubert*. The *Lytle* court clarified when *Daubert* should be utilized to assess the admissibility of expert evidence in Indiana state courts.[216]

In *Lytle*, the court reviewed a trial court's entry of summary judgment in favor of Ford based upon, inter alia, the plaintiff's lack of competent expert evidence on causation.[217] The court noted that "[t]he admissibility of an expert's

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207. *Id.* (quoting Bradley v. Brown, 42 F.3d 434, 437 (7th Cir. 1994) (other citations omitted) (alteration in original)).

208. *Id.* (quoting United States v. Vitek Supply Corp., 144 F.3d 476, 485 (7th Cir. 1998) (other citations omitted)).

209. *Id.* (quoting *Vitek Supply*, 144 F.3d at 485 (other citations omitted)).

210. *Id.* at 516.

211. *Id.* at 517-18.

212. *Id* at 518 (citations omitted).

213. *Id.* (citations omitted).

214. *Id.* at 519.

215. 696 N.E.2d 465 (Ind. Ct. App. 1998).

216. *Id.*

217. *Id.* at 466-67.

testimony is governed by [Indiana Rule of Evidence] 702.'"[218] Accordingly,

> where an expert's testimony is based upon the expert's skill or experience rather than on the application of scientific principles, the proponent of the testimony must only demonstrate that the subject matter is related to some field beyond the knowledge of lay persons and the witness possesses sufficient skill, knowledge or experience in the field to assist the trier of fact to understand the evidence or to determine a fact in issue.[219]

On the other hand, "when the expert's testimony is based upon scientific principles, the proponent of the testimony must also establish that the scientific principles upon which the testimony rests are reliable."[220] Thus, according to *Lytle*, the admissibility standard enunciated in *Daubert* applies only to expert testimony based upon scientific principles.[221]

In *Lytle*, plaintiffs presented experts who testified that the plaintiffs' seat belt both inadvertently and inertially released.[222] The expert opinion regarding inadvertent release was based upon the expert's observations of the buckle and his observations of the configuration of the buckles.[223] The trial court excluded the expert opinion concerning inadvertent release because the testimony did not appear "scientifically based" and there was an insufficient "scientific foundation."[224] On appeal, the Indiana Court of Appeals noted that the expert's testimony was based upon his observations and his knowledge and experience rather than any scientific principles.[225] Therefore, proof of scientific reliability was not required.[226] Nonetheless, the court of appeals upheld the trial court decision excluding the expert evidence because plaintiffs failed to demonstrate that the expert possessed the requisite skill, knowledge, or experience that would

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218. *Id.* at 469. Indiana Rule of Evidence 702 provides:

> (a) If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise.
>
> (b) Expert scientific testimony is admissible only if the court is satisfied that the scientific principles upon which the expert testimony rests are reliable.

IND. R. EVID. 702.

219. *Lytle*, 696 N.E.2d at 469-70 (citing IND. R. EVID. 702(a); Corbin v. State, 563 N.E.2d 86, 92-93 (Ind. 1990)).

220. *Id.* at 470 (citing IND. R. EVID. 702(b)).

221. *Id.*

222. *Id.*

223. *See id.*

224. *Id.*

225. *Id.*

226. *See id.* (citation omitted).

assist the trier of fact in understanding the evidence.[227]

Plaintiffs' expert opinion concerning inertial release was based upon pendulum tests performed in which the experts were able to cause the buckle in question to inertially release by hitting the back of it with a hand or a hammer.[228] The court of appeals concluded that these opinions were based upon "complex scientific principles" and, thus, must have been shown to be scientifically reliable.[229] Because the tests failed to take into consideration web tension, among other things, the Indiana Court of Appeals concluded that they were properly excluded as scientifically unreliable.[230]

227. *Id.* at 470-71.
228. *See id.* at 471.
229. *Id.*
230. *Id.*

SURVEY OF 1998 DEVELOPMENTS IN THE LAW OF PROFESSIONAL RESPONSIBILITY

CHARLES M. KIDD*

During this survey period, a number of notable events occurred highlighting the multi-faceted nature of the law governing lawyering. Developments in the areas of solicitation of legal services, the Interest On Lawyer Trust Accounts program, mishandling client funds, and lawyers elected to public office all served to broaden the spectrum of ethical concerns for Indiana lawyers.

I. INTEREST ON LAWYER TRUST ACCOUNTS ("IOLTA")

Since the Florida Supreme Court created the original IOLTA program in 1978,[1] each of the states has, in turn, enacted their own programs for these funds.[2] IOLTA money, generally, is interest developed from lawyers' trust accounts wherein client funds that are either nominal in amount or held for a short period of time are placed in interest-bearing accounts.[3] The interest generated is paid to state run programs for a number of different public interest activities.[4] Often, the funds are used to provide direct legal services to the indigent, public education programs, and publications about the law.[5]

In 1997, Indiana became the fiftieth state to create an IOLTA program.[6] By amending Indiana's Rules of Professional Conduct, the Indiana Supreme Court created the program to be run by the Indiana Bar Foundation, with the aim of reimbursing expenses (not fees) incurred by Indiana lawyers directly delivering *pro bono* legal services to indigent clients.[7]

As the Indiana formulation began to gel, events elsewhere foreshadowed possible problems for the fledgling program. A Texas case, *Phillips v. Washington Legal Foundation*,[8] had been percolating up through the federal courts for a couple of years. In essence, the plaintiffs in *Phillips* claimed that if the principle sums on which interest was earned belonged to clients, then the interest on the money must, therefore, belong to the clients.[9] They reasoned that the states' IOLTA programs constituted a "taking" under the U.S. Constitution and filed suit to undo the Texas program.[10] The Supreme Court, however,

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* Staff Attorney, Indiana Supreme Court Disciplinary Commission. J.D., 1987, Indiana University School of Law—Indianapolis. The opinions expressed herein are solely those of the author and do not represent a statement of law or policy by the Indiana Supreme Court, any of its staff or attendant agencies.

1. *In re* Interest on Lawyer Trust Accounts, 356 So.2d 799 (Fla. 1978).
2. *See* LAWS. MAN. ON PROF. CONDUCT (ABA/BNA) § 45: 202-5 (1997).
3. *See id.* § 45:201.
4. *See id.*
5. *See id.*
6. *See id.*
7. IND. RULES OF PROFESSIONAL CONDUCT Rule 1.15(d)-(h) (amended 1997).
8. 118 S. Ct. 1925 (1998).
9. *See id.* at 1929.
10. *Id.*

refused to address the "taking" issue, but voiced a clear opinion as to whom the generated interest belonged. The Court held:

> the interest income generated by funds held in IOLTA accounts is the "private property" of the owner of the principal. We express no view as to whether these funds have been "taken" by the State; nor do we express an opinion as to the amount of "just compensation," if any, due respondents. We leave these issues to be addressed on remand. The judgment of the [c]ourt of [a]ppeals is affirmed.[11]

Historically, holding client funds at interest presented a knotty problem for lawyers. Until recently, it was extremely difficult—and not at all cost effective—for lawyers to "sub-account" for interest earned on pooled client funds.[12] For example, assume a lawyer used a single, interest-bearing, "pooled funds" trust account and held $100 for client A for 37 days, $1537 for client B for sixty-two days, and $21,514 for client C for four days. It should be readily apparent that the lawyer's ability to calculate and pay out the correct amount of interest attributable to each of the three clients was very burdensome and prone to error. This problem, of course, was compounded in direct proportion to the size of the firm and the number of clients with funds in the trust account. Because of this inability to sub-account for the interest due, it became part of the "lore of lawyering" that holding client funds at interest was unethical and contrary to disciplinary codes.[13] In truth, there was *never* a specific provision in the current Indiana Rules of Professional Conduct or its predecessor Indiana Code of Professional Responsibility that outlawed the practice of holding client funds at interest.[14] The premise of the IOLTA program avoided the sub-accounting problem by combining client funds that were either a nominal amount or held for a short period of time into one, interest-bearing account.[15] That accumulated interest could then pay into the state IOLTA program with considerably less trouble than attributing amounts to each client.[16]

In the *Phillips* case, the Supreme Court of the United States did not address the issue of whether state IOLTA programs constituted a taking under the U.S. Constitution. Instead, the Court limited its decision to hold only that the interest earned on client funds belonged to the respective clients.[17] The Court then remanded the case back to the district court for a decision on the merits of the "taking" issue.[18] Ultimately, the *Phillips* decision could substantially change the IOLTA environment nationwide.

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11. *Id.* at 1934.

12. *See, e.g.*, *In re* Interest on Lawyers' Trust Accounts, 675 S.W.2d 355, 357 (Ark. 1984).

13. *See id.* at 356-57.

14. *See* IND. RULES OF PROFESSIONAL CONDUCT Rule 1.15 (1998) and the former IND. CODE OF PROF. RESP. DR 9-102 (repealed January 1, 1987).

15. IND. RULES OF PROFESSIONAL CONDUCT Rule 1.15(d) (effective February 1, 1998).

16. *Id.*

17. Phillips v. Washington Legal Found., 118 S. Ct. 1925, 1928 (1998).

18. *Id.* at 1934.

In Indiana, meanwhile, the finalization of the program is on hold by order of the Indiana Supreme Court. On September 30, 1998, the court issued an order[19] holding the effective date for compliance with the applicable rules[20] in abeyance until further order of the court. Under the order, the IOLTA program could not begin operation until it received final approval from the Internal Revenue Service.[21] Although IRS approval was subsequently given, no countermanding order from the Indiana Supreme Court had been issued at the time of this Article's publication.

II. THE CASES

A. Mishandling Client Funds

Mishandling client funds is a perennial source of disciplinary actions against lawyers.[22] During this survey period, one case highlighted two problems: How does one prove such a mishandling occurred and what is an appropriate sanction for the lawyer? *In re Towell*[23] involved a lawyer who both failed to refund unearned legal fees and converted client funds for uses that did not benefit the clients.

In *Towell*, the respondent lawyer was charged with multiple counts of misconduct under the Rules of Professional Conduct. In one count, the lawyer was retained by an elderly woman to handle a matter involving property situated in the state of Wisconsin. During the representation, he came into possession of various papers and documents belonging to the woman. In late February 1993, the client discharged the lawyer. She also directed the lawyer to deliver her files to her banker.[24] The client later sued the lawyer and he counterclaimed for his fees. The lawyer received a judgment on his counterclaim for $3020.[25] After a hearing in December 1993, the client was found in contempt and jailed. She remained in jail for five days until she paid the judgment on December 8, 1993.[26] She thereafter demanded return of her files and, having no response, filed her grievance with the Disciplinary Commission in June 1996.[27]

In another count, the lawyer received a $600 retainer to represent a woman in a dissolution proceeding with the understanding that he would attempt to

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19. *In re* Ind. Professional Conduct Rule 1.15 and Admission and Discipline Rule 23(21), No. 94S00-9809-MS-533 (Ind. Sept. 30, 1998).

20. IND. RULES OF PROFESSIONAL CONDUCT Rule 1.15(d-h) (1998); IND. ADMIS. & DISC. R. 23(21)(c) (1998).

21. *See supra* note 19.

22. *See, e.g., In re* Cochran, 383 N.E.2d 54 (Ind. 1978).

23. 699 N.E.2d 1138 (Ind. 1998).

24. *See id.* at 1139.

25. *See id.*

26. *See id.*

27. *See id.*

secure a court order requiring the client's husband to pay his fees.[28] The final decree was entered June 4, 1993, requiring the ex-husband to pay $3000 to the lawyer for his fees. The ex-husband paid in a timely matter but, despite repeated demands for the return of her retainer, the client did not get her money back until April 1996.[29] In his defense, the lawyer told the client simply that he was having "financial problems."[30]

In still another count, the lawyer was retained to represent a man in his pursuit of a worker's compensation claim. In August 1995, the lawyer entered into a settlement of the client's claim for $23,904.76. He deposited the funds into his escrow account.[31] On September 1, 1995, prior to the client receiving his share, two checks for $250 cleared the account. They were for the benefit of another client's friend and totally unrelated to the worker's compensation client.[32] Later the lawyer used $1035.25 to pay a medical bill of yet another client whose matter was completely unrelated to the workers compensation client's.[33] Although the lawyer was using the settlement proceeds to pay others' bills, he had not paid the chiropractor's bill due from the worker's compensation client.[34] In February 1996, the client filed a grievance with the Disciplinary Commission. He received payment in full from the lawyer in April 1996, some seven months after the settlement proceeds came into the lawyer's hands.[35] The trial court also found that his completely unauthorized use of the client's settlement proceeds constituted conversion as defined in Indiana's criminal code and thereby was a crime reflecting adversely on the lawyer's fitness and character as proscribed by the Indiana Rules of Professional Conduct.[36]

In presenting the case to the supreme court, the lawyer argued that his conduct was, at worst, neglectful and deserving only of a reprimand. He also argued that he should be ordered to take a law practice management course as the remedy for his problems.[37] The Commission argued that any lawyer who misappropriates client funds should be disbarred.[38] The court decided to strike a balance between the two and found:

> It is true that outright theft of client funds generally warrants severe sanction, up to and including disbarment. Those cases demonstrate that where a lawyer knowingly or intentionally steals client or third party funds held in trust for the lawyer's own selfish benefit, that lawyer is

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28. *See id.* at 1140.
29. *See id.*
30. *See id.*
31. *See id.*
32. *See id.*
33. *See id.*
34. *See id.*
35. *See id.*
36. *Id.* at 1141. *See* IND. RULES OF PROFESSIONAL CONDUCT Rule 8.4(b).
37. *See In re Towell*, 699 N.E.2d at 1141.
38. *See id.*

> viewed as being unfit to continue in the profession absent extremely compelling mitigating or extenuating factors. Here, respondent Towell clearly engaged in serious client and third-party fund mismanagement. However, we are convinced that the respondent's mission was not theft of client money. As the respondent explained it, from his "pooled" trust account he unwittingly permitted one client's funds to be used for other, unrelated obligations of other clients and/or third parties in an apparent good faith belief that other client funds would soon arrive to cover the expenditures. We, of course, are not persuaded that the respondent's actions were totally inadvertent, or unwitting; however, we are convinced that he did not intend to deprive his worker's compensation client of the value or use of his funds sufficient to find theft of the funds. What he did was intentionally and without authorization use one client's funds for the benefit of others intending all along to replace the money "very shortly" when the expected "replacement" funds became available. Unfortunately for everyone, the other client funds did not materialize for some time. As a result, the chiropractor's bill remained unpaid, prompting initiation of a disciplinary grievance. That course of events demonstrate an example of the potential pitfalls of poor client fund management.
>
> Nevertheless, the respondent's acts indicate no selfish motive in his inappropriate use of his client's funds. As such, we view his acts as somewhat less culpable than outright theft. However, even in the absence of a finding that the respondent stole his client's money, his gross mishandling of funds held in trust for others nonetheless indicates serious professional shortcomings deserving of significant sanction, primarily for the protection of other clients. Coupled with his callous and arrogant disregard of the Commission's authority and cavalier treatment of his clients' rights and interests upon termination of representation, we conclude that lengthy exclusion from practice is in order.[39]

The supreme court then ordered the lawyer suspended from the bar for a period of eighteen months.[40]

The unique feature of *Towell* is the distinction drawn between the lawyer's misuse of client funds for his personal needs and his misuse of client funds for the needs of others. This suggests that, to the extent possible, misappropriated client funds should be traced to demonstrate clearly and convincingly that money's destination. In *Towell*, the lawyer's use of the funds for others mitigated what would presumably be a more severe sanction for use of the money for himself.[41]

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39. *Id.* at 1141-42 (citations omitted).

40. *Id.*

41. *Id. See also In re* Frosch, 597 N.E.2d 310, 311 (Ind. 1992) (rejecting the suggestion that the lawyer's mishandling of client funds constituted a criminal action because of the lawyer's clear

In contrast, the supreme court decided the case of *In re Stivers*,[42] which also involved misappropriated client funds. In *Stivers*, while the lawyer should have been holding in trust $420 of the client money for expenses, the balance in the account fell below that amount on several occasions.[43] The lawyer explained that the inadequate balances resulted from monthly bank service charges assessed against the trust account balance without reimbursement by the lawyer.[44] In this case, the payout of client funds benefitted the lawyer to some extent.[45] The lawyer in *Stivers* received a two year suspension from the bar.[46]

In the same vein, the lawyer in *In re Campbell*[47] received an eighteen month suspension when he took $2000 for litigation expenses, deposited the money in his personal account when it should have been in trust, then abandoned his practice and took the client's funds with him.[48] Although the lawyer did not show up for his disciplinary hearing, he was still found to have committed a criminal act and ordered to make restitution before being eligible to petition for reinstatement to the bar.[49]

B. Self-interest and the Lawyer in Public Office

Two disciplinary cases involving lawyers holding public office merit attention by all members of the bench and bar. They are *In re Edwards*[50] and *In re Riddle*.[51] Both lawyers held public office (a judge and prosecutor, respectively) and both were disbarred. Although each has the common element of an elected lawyer,[52] there is an important ethics lesson for all lawyers laying behind the obvious ethical implications for public office holders who engage in self-dealing. These two cases echo sentiments advanced by the supreme court for almost twenty years.

In *Edwards*, the respondent lawyer was charged with personal misconduct in a number of counts. In at least two instances, the respondent engaged in sexual relationships with clients during the course of his representation.[53] In one instance, he created a fake dissolution decree on which the client relied in her

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fee dispute with the client).

42. 683 N.E.2d 1312 (Ind. 1997).
43. *See id.* at 1313.
44. *See id.*
45. *See id.*
46. *See id.* at 1314.
47. 702 N.E.2d 692 (Ind. 1998).
48. *See id.* at 693-94.
49. *See id.* at 693.
50. 694 N.E.2d 701 (Ind. 1998).
51. 700 N.E.2d 788 (Ind. 1998).
52. Disciplinary action against lawyers holding elected office is nothing new. *See, e.g.*, *In re* Curtis, 656 N.E.2d 258 (Ind. 1995); *In re* Moerlein, 520 N.E.2d 1275 (Ind. 1988); *In re* Holovachka, 198 N.E.2d 381 (Ind. 1964).
53. *See Edwards*, 694 N.E.2d at 705, 708.

dealings with others.[54] In another case, Edwards served as presiding judge in a case without disclosing that he had a prior attorney-client relationship with the husband and wife defendants.[55] Still further, Edwards was appointed as a judge pro tempore in Delaware County Superior Court in the spring of 1996. He continued to accept his full pay as a part-time deputy city attorney for the city of Muncie even though he was receiving pay as a full time judge.[56] Later that year, when he stood for re-election to the superior court bench he was holding, he continued to represent the city in legal matters *and* undertook new representations in his private law office.[57] Even more remarkably, Edwards also maintained a position as a part-time probate commissioner in the Henry County probate court, despite his election to a full-time judgeship in the adjacent county.[58]

In *Riddle*, the respondent lawyer was the elected prosecuting attorney for Crawford County, Indiana, having taken office in January 1995.[59] Initially, Riddle served as the part-time prosecuting attorney[60] and simultaneously maintained a private practice with an office in the small town of Marengo.[61] His private practice consisted of a group of bank and title company clients for whom Riddle did title work at a flat rate of $100 for title opinions plus incidental costs. Riddle hired a lawyer named Evans on the promise that Evans would work in Riddle's private office and also serve as Chief Deputy Prosecutor for that county. As permitted by statute,[62] Riddle chose to become full time prosecutor on January 1, 1996, which entitled him to a state-paid salary of $85,000 per year with the proviso that he devote his full energies to representing the state of Indiana and maintain no private law practice. A week later, Evans began working in Riddle's private law office as a partner with Riddle. The same day, Evans was appointed Chief Deputy, signed his oath of office, and went on the state payroll. The Riddle law office signage, office secretary, and letterhead remained essentially unchanged. In a newspaper interview, Riddle did not reveal that Evans had anything to do with the prosecutor's office and no formal announcement was made regarding Evans' appointment. In August 1996, Riddle summoned Evans to the Crawford Circuit Court's office for a second swearing-in ceremony to be performed by the judge. Prior to that time, Evans had done no prosecutions nor any significant work for the prosecutor's office. No one mentioned Evans' prior appointment in January when the circuit judge swore him in a second time in

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54. *See id.* at 705.

55. *See id.* at 709.

56. *See id.* at 714.

57. *See id.* at 714-15.

58. *See id.* Based on the misconduct, the factual development is quite extensive.

59. *In re* Riddle, 700 N.E.2d 788, 790 (Ind. 1998).

60. This has been permissible in Indiana for some time. Indiana has a specific rule to guard against the dangers of conflict of interest for part-time prosecutors and deputies. *See* IND. RULES OF PROFESSIONAL CONDUCT Rule 1.8(k) (amended 1986).

61. *Riddle*, 700 N.E.2d at 790.

62. IND. CODE § 33-14-19.5 (1998).

August. Evans had no desk at the court house, was assigned no work or investigations, and had received no training. Although Riddle later testified that Evans performed vast amounts of research, he was unable to produce anything that Evans had done for the prosecutor's office. During the year when Evans ran the Riddle law office, Riddle made almost $35,000 from his private practice while Evans received only $540.[63] Riddle was later charged both in his disciplinary case and in a criminal action with having committed ghost employment[64] and, on the basis of that misconduct and its attendant violations, was disbarred.[65]

Obviously, the actions of both lawyers in *Edwards* and *Riddle* represented clear cases of self-dealing while holding public office, which was, of course, intolerable to the supreme court. The court's observations, however, are worthy of additional analysis. In *Edwards*, the court noted:

> The pertinent facts found by the Masters to have been clearly and convincingly proven are summarized below. In some instances, the factual testimony of Respondent was in conflict with the testimony of others. In their report, the Masters expressly stated, "Wherever in the record of proceedings the testimony of Judge Joseph G. Edwards contradicts the testimony of other witnesses we find that his testimony regarding such matters is less credible than the testimony of other witnesses." The Masters were in the best position to observe and assess witness credibility and their judgment in reconciling conflicting evidence carries great weight.[66]

This would be a remarkable finding under any circumstance, but the respondent lawyer in *Edwards* simultaneously held positions of high trust within his community. Similarly, in *Riddle*, the court found:

> At the hearing of these disciplinary charges, the respondent testified under oath that Evans performed vast amounts of research for the Crawford County prosecutor's office between January 8 and August 5, 1996. He was unable to support that contention with a single iota of corroborating evidence. In fact, other employees of the office testified in substance that to their knowledge Evans essentially did no work for the office during this period. Evans himself also testified to that effect. We therefore find that the respondent's contrary statements at the hearing were knowingly false and, therefore, violative of [Professional Conduct Rule] 8.1(a). Similarly, by stating that he received no fees from the Riddle Law Office after electing full-time status as prosecuting attorney of Crawford County when he had, in fact, received almost

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63. *See Riddle*, 700 N.E.2d at 790-92.

64. IND. CODE § 35-44-2-4.

65. *See Riddle*, 700 N.E.2d at 786.

66. *In re* Edwards, 694 N.E.2d 701, 704 (Ind. 1998) (citing *In re* Frosch, 643 N.E.2d 902, 904 (Ind. 1994)).

> $35,000 in net proceeds from Evans' preparation of title opinions, the respondent again violated [Professional Conduct Rule] 8.1(a).[67]

The court's finding was very similar to that in *Edwards*: The lawyer's word carried no greater presumption of truthfulness than that of any other witness in the proceeding.

Findings of this type go far back in the line of disciplinary cases. In *In re Barefoot*,[68] the court held:

> Accordingly, we will proceed with the review process, whereby we examine all matters presented, including the Hearing Officer's findings and conclusions. Although such findings are not binding on this Court,[69] they do receive emphasis due to the Hearing Officer's unique opportunity for direct observation of the witnesses.[70]
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> * * *
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> We are not persuaded by Respondent's unsubstantiated, self-serving contentions. We conclude, as did the Hearing Officer, that the Respondent, by using as his own, client's funds entrusted to him for payment of inheritance taxes, engaged in criminal conversion in violation of Indiana Code [section] 35-43-4-3.[71]

The lawyer in *Barefoot* was disbarred.[72]

Later, in *In re McDaniel*,[73] the problem of lawyer self-interest rose again. In that case, the lawyer, as manager of the local license branch had, inter alia, created a fictitious person, paid her a weekly salary, and then pocketed the money himself. Again the court held:

> Although this Court is not bound by the findings tendered by the Hearing Officer, such findings do receive emphasis in that the Hearing Officer observes the witnesses, absorbs the nuances of unspoken communication, and by this observation attaches credibility to the testimony.
>
> In this case, Respondent's testimony is in conflict with other evidence presented in this cause. The Hearing Officer chose not accept all of the Respondent's representations. The record presented for review supports the findings of the Hearing Officer.[74]

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67. *Riddle*, 700 N.E.2d at 794.
68. 533 N.E.2d 128, 129 (Ind. 1989).
69. Because the supreme court's jurisdiction in disciplinary proceedings is plenary, their review of the findings made at trial is de novo. *See In re* Barnes, 691 N.E.2d 1225 (Ind. 1998); *In re* Towell, 690 N.E.2d 1138 (Ind. 1998).
70. *In re Barefoot*, 533 N.E.2d at 129 (citations omitted).
71. *Id.* at 133.
72. *See id.*
73. 470 N.E.2d 1327 (Ind. 1984).
74. *Id.* at 1328 (citation omitted).

One respondent lawyer suggested that the Hearing Officer's refusal to believe his version constituted an impermissible shifting of the burden of proof. In *In re Kerr*,[75] the respondent lawyer mishandled a client's tax refund over a period of time requiring the client to seek judicial resolution of his claim against the lawyer. In the underlying representation, Kerr was made personally responsible for paying the client's new lawyer to recover his money for him. In discounting the lawyer's credibility, the court admonished:

> The Respondent insists that because the hearing officer did not adopt Respondent's explanations as findings of fact, somehow the burden of proof was shifted upon him to prove his innocence. Respondent confuses the concepts of the shifting of the burden of proof with the hearing officer's obligation to weigh conflicting evidence, including the credibility of a witness who takes the witness stand in his own behalf.[76]

The message, then, seems clear. Lawyers who speak in their own defense would be well advised to offer solid corroboration beyond their own testimony. *Edwards* and *Riddle* confirm that self-serving testimony in a case with an allegation of self-dealing will be given little, if any, weight. In addition, the court also decided *In re Brooks*[77] with many of the same issues involving the misappropriation of client funds as described above. In *Brooks*, the lawyer received a nine month suspension from the bar.[78] Like the other cases discussed herein, the lawyer offered defenses as to the misappropriation charges, but due to his uncorroborated testimony, the court found his defenses unpersuasive, thereby accepting the hearing officer's conclusions on credibility.[79]

In each of the cases described herein the respondent lawyers had no proof that their actions were in any way motivated by a reason other than personal gain. Although free to demonstrate otherwise, lawyers cannot rely on the strength of their own words in proving their motivations. As the court has observed, this close scrutiny does not constitute a burden shift, but merely a critical examination of the evidence—or lack thereof—to support the lawyer's version of events.

C. *The Scope of a Lawyer's Authority*

During this survey period, a pair of cases addressed the issue of whether an attorney has the implied authority to settle a civil case without the authorization or consent of the client. The treatments given by both the Indiana Court of Appeals and the Indiana Supreme Court are very illuminating for all lawyers.

In *Red Arrow Ventures, LTD v. Miller*,[80] the Fifth District of the Court of

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75. 640 N.E.2d 1056 (Ind. 1994).
76. *Id.* at 1058.
77. 694 N.E.2d 724 (Ind. 1998).
78. *See id.* at 729.
79. *Id.* at 726.
80. 692 N.E.2d 939 (Ind. Ct. App. 1998).

Appeals was presented with a situation where a settlement was enforced against defendants in a civil case based upon the actions of the their attorney. In *Red Arrow*, suit was commenced for breach of a promissory note wherein the defendants had stopped making payments. After a failed attempt at mediation, the case was tried over the course of three days in May 1996. At the end of the trial, the judge announced that he would rule against the defendants on the issue of liability, but he did not mention the amount of damages he would award Miller. Over the next couple of days, the lawyers for the parties met and discussed a settlement of the case. They arrived at a proposed settlement of $21,000 and, in follow-up correspondence, the defendant's lawyer memorialized the agreement and the mechanism by which it would be paid. A few weeks later, the defendant's lawyer communicated that his clients did not want to pay the settlement. Because the settlement was not in the plaintiff's hands by the end of July 1996, the plaintiff filed a motion to enforce the settlement and for attorney's fees. The court ultimately bound the defendants to the settlement and ordered them to pay an additional $1000 in attorney fees.[81]

The court of appeals reviewed a long line of Indiana cases holding that attorneys have the apparent authority to settle a claim without the consent of the client. The Fifth District opinion, however, wrestled with the court's analysis in *Gravens v. Auto-Owners Insurance Co.*,[82] which held that the client has the ultimate authority to decide when to settle a civil case.[83] Ultimately, the court of appeals held:

> We believe that our supreme court's decision in *Ferrara v. Genduso*[84] . . . clearly stands for the proposition that a settlement agreement into which an attorney enters is enforceable against his client who has not consented to be bound by it. We note that "the Court of Appeals is obliged to follow the precedents established by the Indiana Supreme Court." We therefore hold that, when an attorney enters into a settlement agreement without his client's consent, the agreement is enforceable against the non-consenting client. We disapprove of *Klebes* and *Gravens* to the extent they conflict with our holding.[85]

The court then went on to vacate the award of attorney fees to the plaintiff's lawyers as not authorized by prior law.[86]

At the same time *Gravens* and *Red Arrow* were working their way through the court of appeals, the federal case of *Koval v. Simon-Telelect, Inc.*[87] was wrestling with a similar problem involving a lawyer's ability to bind a client to a settlement after the client balked. In August 1997, the U.S. District Court in

81. *Id.* at 946.
82. 666 N.E.2d 964 (Ind. Ct. App. 1996).
83. *Id.* at 966.
84. 14 N.E.2d 580 (Ind. 1938).
85. *Red Arrow Ventures*, 692 N.E.2d at 945-46 (citation omitted).
86. *Id.* at 947.
87. 979 F. Supp. 1222 (N.D. Ind. 1997).

the South Bend division certified two questions of law to the Indiana Supreme Court:

> 1. If an attorney settles a claim as to which the attorney has been retained, but does so without the client's consent, is the settlement binding between third parties and the client?
>
> 2. Under the portion of [Indiana] Code [section] 22-3-2-13 that provides, "consent shall not be required where the employer or the employer's compensation insurance carrier has been fully indemnified or protected by court order," does it constitute "protection by a court order" such that consent is not required for the settlement of claims and satisfaction of judgment in proceedings, for the court to specifically preserve a compensation insurance carrier/lienholder's right to bring suit against its agent for settling its claim while enforcing an oral settlement of claims by reason of injury or death?[88]

A week after the court of appeals decision in *Red Arrow*, the Indiana Supreme Court issued an answer to the certified questions in the Indiana case of *Koval v. Simon-Telelect, Inc.*[89] In a scholarly opinion by Justice Boehm, the supreme court examined an attorney's implied authority, an attorney's apparent authority, and an attorney's inherent agency power in court proceedings.[90] In the end, the court held:

> We conclude that a client's retention of an attorney does not in itself confer implied or apparent authority on that attorney to settle or compromise the client's claim. However, retention does confer the inherent power on the attorney to bind the client to an in court proceeding. For purposes of an attorney's inherent power, proceedings that are regulated by the [Indiana Rules for Alternative Dispute Resolution][[91]] in which the parties are directed or agree to appear by settlement authorized representatives are in court proceedings. We also conclude that for purposes of Indiana Code [section] 22-3-2-13 it does not constitute "protection by court order" for a court specifically to preserve an employer's or an employer's insurance carrier's right to bring suit for breach of duty by its agent.[92]

What then, of the client's rights that his lawyer has compromised? Those rights become a potential malpractice claim against the lawyer.

An attorney may without express authority bind his client by agreement

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88. *Id.* at 1232.

89. 693 N.E.2d 1299 (Ind. 1998).

90. *Id.* at 1302-07.

91. IND. RULES FOR ALTERNATIVE DISPUTE RESOLUTION (as amended through February 1, 1998).

92. 693 N.E.2d 1309-10.

> that judgment may be taken against him, and that, too, though the attorney know that his client has a good defense to said action. If [the attorney] acts contrary to the express directions of his client, or to his injury, the client must look to the attorney for redress. Although the theoretical underpinnings of this rule are not always fully explained, and on occasion are set forth in terms slightly at variance with standard agency doctrines, these cases uniformly bind the client to an in court agreement by the attorney and remit the client to any recovery that may be available from the attorney. This distinction between in court consents and out of court agreements is also found in Indiana statutory law at least since the civil code of 1881 and currently embodied in Indiana Code [section] 34-1-60-5: "An attorney has authority, until discharged or superceded by another . . . [t]o bind his client in an action or special proceeding, by his agreement, filed with the clerk, or entered upon the minutes of the court, and not otherwise." Although the statute perpetuates the archaic term "minutes of the court" today it presumably refers to the transcript and chronological case summary and, in the context of an [Alternative Dispute Resolution], whatever memorializes that proceeding.
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> * * *
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> Indeed one rarely encounters a rule that is so commonly cited and yet so infrequently explained.[93]

Thereafter, the court examined the need to vest such authority in attorneys. In essence, lawyers in trial offer evidence and make arguments that invariably bind their clients to a particular position. It is the desire of the court to foster resolution of disputes without resort to trial; the logic of holding that mediation proceedings are "in-court" matters predictably follows.[94]

The *Koval* and *Red Arrow* cases bear close reading by all practicing lawyers. These two cases, and those cited therein, give an important outline of the lawyer's power in dealing on behalf of clients. At the very least, they suggest that not only should the lawyer know the limits of his authority, but he should confer regularly with his client to create clear boundaries for the course of the representation.

II. Rule Amendments of Note

A. Pro Hac Vice *Admission*

The methods by which attorneys are admitted to the bar (and disciplined as well) are described in the Indiana Rules of Admission to the Bar and the Discipline of Attorneys.[95] With the exception of some minor amendments in

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93. *Id.* at 1305-06. This last comment is the product of case research going as far back into British jurisprudence as 1699.

94. *See id.* at 1307.

95. The various individual rules have been promulgated by the supreme court through the

1990, the rule on *pro hac vice* admission has remained essentially unchanged since its original adoption. In 1999, however, the rule received a major overhaul.

In the past, the question of *pro hac vice* admission was a matter within the discretion of the presiding judge.[96] Beyond that, there were few objective standards on which a court could reject such a request. The new formulation of the rule requires that the presiding judge make certain findings to justify the foreign attorney's temporary admission. The judge must find, inter alia, that a member of the Indiana bar has appeared and agreed to act as co-counsel, that the foreign attorney is not a resident of the state, regularly employed in Indiana, or regularly engaged in business or professional activities in the state.[97] In addition, the foreign attorney must file a verified petition reciting a number of averments including his residence, his standing in his home jurisdiction's bar, and a list of all Indiana proceedings in which he is participating.[98] Additionally, the clerk of the Indiana Supreme Court must now keep what is essentially a "registry" of all attorneys who appear *pro hac vice* in Indiana proceedings.[99] The full text of the new rule is set out in Appendix A.

B. *Mandatory Continuing Legal Education*

The primary change in the rule[100] governing mandatory continuing legal education involves new admittees to the Indiana bar. For those new lawyers admitted in 1999 and thereafter, each must obtain continuing legal education from the beginning of their careers.[101] Since the rule's inception, new admittees were granted a three-year grace period from their admission before they had to attend continuing education seminars.[102] Under the amendment, new admittees will have to complete "programs designated by the Commission as appropriate for new lawyers."[103] That class of programs is not, as yet, defined by rule. The educational requirements for all other lawyers remains unchanged. The text of the new rule follows this article as Appendix B.

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years and were ultimately collected in this body referred to colloquially as the IND. ADMIS. & DISC. RULES. The Oath of Attorneys, for example, was adopted by the Indiana Supreme Court in 1954, but finds its roots in the CANONS OF THE AMERICAN BAR ASSOCIATION, adopted on August 27, 1908.

96. *See, e.g.*, Michael A. Disabatino, Annotation, *Attorney's Right to Appear Pro Hoc Vice in State Court*, 20 A.L.R. 4TH 855 (1981).

97. IND. ADMIS. & DISC. R. 3 §§ 2 (a)(1) & (2) (as amended 1999). See *infra* Appendix A for rule text.

98. IND. ADMIS. & DISC. R. 3 § 2(a)(3) (as amended 1999).

99. IND. ADMIS. & DISC. R. 3 § 2(b) (as amended 1999).

100. IND. ADMIS. & DISC. R. 29 § 3 (as amended 1999).

101. IND. ADMIS. & DISC. R. 29 § 3(a) (as amended 1999).

102. IND. ADMIS. & DISC. R. 29 § 3(b) (as amended 1999).

103. *Id.*

C. *Oversight of Lawyer Trust Accounts*

In 1997, the supreme court created the Indiana Supreme Court Disciplinary Commission Rules Governing Attorney Trust Account Overdraft Reporting. These six rules regulated the methodology by which financial institutions in Indiana qualified to keep attorney trust accounts and agreed to report overdrafts on such accounts.[104] By amending the rules during this survey period, the supreme court tailored the rules to more closely fit existing practice. The court recognized that, in many instances, lawyers and law firms keep non-lawyer support staff members as signatories on the office's trust account. In some cases, this practice is not only necessary, but desirable.[105] Although the lawyers in the firm can delegate this authority, they cannot delegate the responsibility for the acts of their staff or the integrity of their trust account management practices.[106] To safeguard lawyers' handling of client funds, the court will now require that the firm use certain safeguards to insure that the trust account is run properly. At a minimum, the bank statements for the trust account must be delivered unopened and reviewed by a supervising attorney. In addition, the reconciliation of the trust account must be done by a person who has no signature authority over the account.[107] The full text of the new requirements follows this article as Appendix C.

D. *Electronic Access*

A growing number of counties throughout the state are making records available through electronic means via their clerk's office. The supreme court amended Trial Rule 77[108] to authorize electronic posting of court records and the mechanism by which fees for records can be obtained. The text of the new rule follows this article as Appendix D.

CONCLUSION

The supreme court and its Disciplinary Commission address problems involving lawyer trust accounts and continually refine the rules and practices used by the bar to hold client funds in trust. Advances have been made in this area through both rule amendments and through disciplinary action to improve accountability to clients. Lawyers also have significantly more guidance as to the

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104. IND. SUP. CT. DISC. COMM. R. GOV. ATT'Y TRUST ACCOUNT OVERDRAFT REP., Rules 1-6 (1997 version) [hereinafter DISC. COMM. R.].

105. This can be particularly true in "form driven" practices, such as bankruptcy and probate in which filing fees or similar expense money is routinely held in trust until the initial documents are ready for filing. In those circumstances, it might provide better service to clients if a legal assistant can sign trust checks rather than holding up document processing to wait on a lawyer signatory.

106. IND. RULES OF PROFESSIONAL CONDUCT Rule 5.3 (1998).

107. DISC. COMM. R. 6(D) (as amended 1999).

108. IND. R. TR. P. 77(K) (as amended 1999).

scope of their authority whether it be apparent, inherent, or implied. The court also significantly formalized the process by which *pro hac vice* admission is conducted. Hopefully, these new rules amendments will provide a more objective standard for courts to make the decision as to whether to admit a foreign lawyer to practice.

APPENDIX A

RULE 3. ADMISSION OF ATTORNEYS

Section 1. Admission of Attorneys.

The Supreme Court shall have exclusive jurisdiction to admit attorneys to practice in Indiana. Admission by the Court shall entitle attorneys to practice in any of the courts of this state.

Section 2. Limited Admission on Petition.

(a) Requirements for Limited Admission on Petition.

A member of the bar of another state or territory of the United States, or the District of Columbia, may appear in the Supreme Court, the Court of Appeals, the Tax Court, or the trial courts of this state in any particular proceeding, if the court before which the attorney wishes to appear determines that there is good cause for such appearance and each of the following conditions is met:

(1) A member of the bar of this state has appeared and agreed to act as co-counsel.

(2) The attorney is not a resident of the state of Indiana, regularly employed in the state of Indiana, or regularly engaged in business or professional activities in the state of Indiana.

(3) The attorney files a verified petition stating:

(i) The attorney's residential address, office address, and the name and address of the attorney's law firm or employer, if applicable;

(ii) The states or territories in which the attorney has ever been licensed to practice law, including the dates of admission to practice and any attorney registration numbers;

(iii) That the attorney is currently a member in good standing in all jurisdictions listed in (ii);

(iv) That the attorney has never been suspended, disbarred or resigned as a result of a disciplinary charge, investigation, or proceeding from the practice of law in any jurisdiction; or, if the attorney has been suspended, disbarred or resigned from the practice of law, the petition shall specify the jurisdiction, the charges, the address of the court and disciplinary authority

which imposed the sanction, and the reasons why the court should grant limited admission not withstanding prior acts of misconduct;

(v) That no disciplinary proceeding is presently pending against the attorney in any jurisdiction; or, if any proceeding is pending, the petition shall specify the jurisdiction, the charges and the address of the disciplinary authority investigating the charges. An attorney admitted under this rule shall have the continuing obligation during the period of such admission promptly to advise the court of a disposition made of pending charges or the institution of new disciplinary proceedings;

(vi) A list of all proceedings, including caption and cause number, in which the attorney, or any member of a firm with which the attorney is currently affiliated, has appeared in any of the courts of this state during the last five years. Absent special circumstances, repeated appearances by any person or by members of a single law firm pursuant to this rule shall be cause for denial of the petition;

(vii) A demonstration that good cause exists for the appearance. Good cause shall include at least one of the following:

(a) the cause in which the attorney seeks admission involves a complex field of law in which the attorney is a specialist, or

(b) there has been an attorney-client relationship with the client for an extended period of time, or

(c) there is a lack of local counsel with adequate expertise in the field involved, or

(d) the cause presents questions of law involving the law of the foreign jurisdiction in which the applicant is licensed, or

(e) such other reason similar to those set forth in this subsection as would present good cause for the *pro hac vice* admission.

(viii) A statement that the attorney has read and will be bound by the Rules of Professional Conduct adopted by the Supreme Court, and that the attorney consents to the jurisdiction of the State of Indiana, the Indiana Supreme Court, and the Indiana Supreme Court Disciplinary Commission to resolve any

disciplinary matter that might arise as a result of the representation.

(ix) A statement that the attorney will file a Notice of *Pro Hac Vice* Admission with the clerk of this court in compliance with Section (b) of this rule within thirty (30) days after the court grants permission to appear in the proceeding.

(b) Notice of *Pro Hac Vice* Status.

All attorneys admitted *pro hac vice* under the provisions of Section 2(a) shall file a Notice with the clerk of this court within thirty (30) days after a court grants permission to appear in the proceeding. Failure to file the notice within the time specified will result in automatic exclusion from practice within this state. The notice shall include the following:

(1) A current statement of good standing issued to the attorney by the highest court in each jurisdiction in which the attorney is admitted to practice law;

(2) A copy of the verified petition requesting permission to appear in the court proceedings, along with the court order granting permission;

(3) A list of all grievances, petitions, or complaints filed against the attorney with any disciplinary authority of any jurisdiction with the determination thereon.

(c) Registration Fee for Attorney Admitted Pro Hac Vice.

The attorney shall pay, during the pendency of the proceedings, the annual registration fee required of members of the bar of this state as set out in Admission and Discipline Rule 23, Section 21.

(d) Responsibilities of Attorneys.

Members of the bar of this state serving as co-counsel under this rule shall sign all briefs, papers and pleadings in the cause and shall be jointly responsible therefor. The signature of co-counsel constitutes a certificate that, to the best of co-counsel's knowledge, information and belief, there is good ground to support the signed document and that it is not interposed for delay or any other improper reason.

APPENDIX B

RULE 29. MANDATORY CONTINUING LEGAL EDUCATION

Section 3. <u>Education Requirements</u>

(a) Every attorney and every judge of a city, town or Marion County small claims court, who is not licensed as an attorney, shall complete no less than six (6) hours of approved continuing legal education each year and shall complete no less than thirty-six (36) hours of approved continuing legal education each Educational Period. At least three (3) hours of approved continuing legal education in professional responsibility shall be included within the hours of continuing legal education required during each three (3) year Educational Period. Such hours may be integrated as part of a substantive program or as a free standing program. All credits for a single educational activity will be applied in one (1) calendar year. No more than twelve (12) hours of the Educational Period requirement shall be filled by Non Legal Subject Matter Courses.

(b) Attorneys admitted to the Indiana Bar before December 31, 1998, on the basis of successfully passing the Indiana Bar examination, shall have a grace period of three (3) years commencing on January 1 of the year of admission and then shall commence meeting the minimum yearly and Educational Period requirements thereafter. Attorneys admitted after December 31, 1998, shall commence meeting the yearly and Educational Period requirements starting on January 1 after the year of their admission by completing programs designated by the Commission as appropriate for new lawyers.

(c) Attorneys admitted on foreign license or attorneys who terminate their inactive status shall have no grace period. Their first three year Educational Period shall commence on January 1 of the year of admission or termination of inactive status.

(d) For judges of city, town and Marion County small claims courts, who are not attorneys, the first three year Educational Period shall commence on January 1 of the first full calendar year in office.

A judge who fails to comply with the educational requirements of this rule shall be subject to suspension from office and to all sanctions under Section 10. A judge so suspended shall be automatically reinstated upon compliance with Section 10(b) "Reinstatement Procedures". The Commission shall issue a statement reflecting reinstatement which shall also be sent to the clerk to show on the Roll of Attorneys that the judge is in good standing.

APPENDIX C

INDIANA SUPREME COURT DISCIPLINARY COMMISSION RULES GOVERNING ATTORNEY TRUST ACCOUNT OVERDRAFT REPORTING

RULE 6. MISCELLANEOUS MATTERS

D. Admission and Discipline Rule 23, section 29(a)(6) contemplates that a designee who is not admitted to practice law in Indiana may be an authorized signatory on a trust account. In the event an attorney or law firm delegates trust account signature authority to any person who is not admitted to practice law in Indiana, such delegation shall be accompanied by specific safeguards, including at a minimum the following:

a. All periodic account activity statements form the financial institution shall be delivered unopened to and reviewed by an attorney having supervisory authority over the non-attorney signatory; and

b. Responsibility for conducting periodic reconciliations between internal trust account records and periodic trust account activity statements from the financial institution shall be vested in a person who has no signature authority over the trust account.

E. All communications from financial institutions to the Disciplinary Commission shall be directed to: Executive Secretary, Indiana Supreme Court Disciplinary Commission, 115 West Washington Street, Suite 1060, Indianapolis, Indiana 46204.

APPENDIX D

RULE 77. COURT RECORDS

K. **Electronic Posting of Court Records**. The clerk, with the consent of the majority of the judges in the courts of record, may make court records, including but not limited to the chronological case summary, record of judgments and orders, index, and case file, available to the public through remote electronic access such as the Internet or other electronic method. The records to be posted, the specific information that is to be included, its format, pricing structure, if any, method of dissemination, and any subsequent changes thereto must be approved by the Division of State Court Administration under the direction of the Supreme Court of Indiana. Such availability of court records shall be subject to applicable laws regarding confidentiality.

RECENT DEVELOPMENTS IN PROPERTY LAW

MICHAEL A. DORELLI*
JOSEPH C. BOWMAN**

INTRODUCTION

During the period covered by this Article,[1] Indiana courts addressed many issues concerning traditional areas of property law. From claims of adverse possession to disputes over water rights, the courts had opportunities to clarify the status of long-standing rules of law, to provide innovative interpretation to novel legal theories, and even to overrule antiquated tenets of property law. The most significant decisions impacting property law are discussed herein.

I. ADVERSE POSSESSION

Adverse possession is a "strange and wonderful system, whereby the occupation of another's land gains the occupier title . . . ."[2] To gain title, the occupier must demonstrate "actual, visible, notorious, and exclusive possession of the real estate, under a claim of ownership hostile to the true owner for a continuous ten-year period."[3] Because any adverse possession claim is bound to be highly fact-sensitive, it is not surprising that several decisions addressing the elements of such a claim reached the appellate level during the survey period.

In *Thompson v. Leeper Living Trust*,[4] the Indiana Court of Appeals was faced with a multi-party dispute over the findings of a legal survey of the parties' adjoining tracts of property. Property owned by the Thompsons was bordered on the east by property owned by Gardner and on the west by a tract owned by Salyer. A tract of land owned by the Leeper Living Trust ("Leeper") extended along the southern border of each of these tracts.[5] The Thompsons and Gardner appealed the survey on an adverse possession theory, claiming that "the boundary line between their tracts and Leeper's tract should have been located farther south than [the] survey indicated because they had acquired, by adverse possession, a 10-to-12-foot-wide strip of land between their tracts and Leeper's

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* Associate, Henderson, Daily, Withrow & DeVoe. B.S., 1994, Indiana University—Bloomington; J.D., *magna cum laude*, 1998, Indiana University School of Law—Indianapolis.

** Associate, Baker & Daniels. B.S., 1992, Indiana University—Bloomington; J.D., *magna cum laude*, 1998, Indiana University School of Law—Indianapolis.

1. This Article surveys decisions handed down by Indiana courts between October 1, 1997 and September 30, 1998.

2. ROGER A. CUNNINGHAM ET AL., THE LAW OF PROPERTY § 11.7, at 807 (2d ed. 1993).

3. Rieddle v. Buckner, 629 N.E.2d 860, 862 (Ind. Ct. App. 1994); *see also* Estate of Mark v. H.H. Smith Co., 547 N.E.2d 796, 799 (Ind. 1989). Section 34-11-2-11 of the Indiana Code provides that "[a]n action . . . for the recovery of the possession of real estate[] must be commenced within ten (10) years after the cause of action accrues." IND. CODE § 34-11-2-11 (1998).

4. 698 N.E.2d 395 (Ind. Ct. App. 1998).

5. *See id.* at 396.

tract."[6]

For well over the ten-year statutory period, a woven wire fence extended along the full length of the boundary between the Leeper tract of land and the tracts owned by Gardner and the Thompsons. In 1995, Leeper removed the fence and replaced it with a barbed-wire fence, which was positioned approximately ten to twelve feet north of the woven wire fence's prior position.[7]

Gardner based his adverse possession claim on four grounds: 1) the location of the woven wire fence; 2) his belief that the woven wire fence marked the true boundary between the tracts; 3) that he utilized the disputed strip of land as a driveway for use by trucks in the operation of his grain storing business; and 4) that he stored certain machinery on the disputed strip.[8] The court rejected all four grounds.[9]

The court quickly dismissed the first two grounds offered by Gardner, stating that "[n]either the fact that the woven wire fence stood where it did, nor the fact that Gardner believed his property extended to the fence, can decisively show that he actually, visibly, notoriously, or exclusively possessed the disputed strip."[10] In making such a conclusory disposition of the issue, the court took a relatively strict stance toward the establishment of an adverse possession claim, evidently granting little weight to the existence of a fence marking an apparent boundary.[11]

The court then found that the third and fourth grounds cited by Gardner also failed to support an adverse possession claim, stating that "periodic or sporadic acts of ownership are not sufficient to constitute adverse possession."[12] The court concluded that the trucks' use of the disputed strip of property could be characterized "at best" as periodic or sporadic use and that the storage of obsolete farm machinery on the tract was equally "intermittent."[13] In drawing

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6. *Id.* at 397. The court also addressed a challenge to the survey based on the survey's variance with the legal description of the property at issue. *Id.* In rejecting portions of the survey, the trial court noted that "the legal description is presumed correct and that compelling visual evidence at variance with the legal description must exist to support a legal survey which varies from a proper legal description." *Id.* The court of appeals affirmed the trial court's decision, granting deference to the trial court's ability to "credit evidence of the survey's inaccuracy and to discount evidence to the contrary." *Id.* at 397-98.

7. *See id.* at 398.

8. *See id.*

9. *Id.*

10. *Id.*

11. *See* CUNNINGHAM ET AL., *supra* note 2, at 809 (recognizing that in many jurisdictions, "[e]nclosure of the land, perhaps even use of it up to some natural physical boundary, introduces an important factor favorable to the possessor") (citing Whittemore v. Amator, 713 P.2d 1231 (Ariz. 1986); Miceli v. Foley, 575 A.2d 1249 (Md. Ct. Spec. App. 1990)).

12. *Thompson,* 698 N.E.2d at 398 (citing McCarty v. Sheets, 423 N.E.2d 297, 301 (Ind. 1981)).

13. *Id.* (quoting Ferguson v. Prince, 190 S.W. 548, 549 (Tenn. 1916) (holding that the evidence failed to sustain a claim of adverse possession where the claimant's supposed possession

this conclusion, the court distinguished *Smith v. Brown*,[14] which found that adverse possession had been established

> where the evidence showed, among other things, that the adverse possessor "trimmed the shrubbery, mowed the grass, and planted flowers on the land in dispute," that he "used the entrance and driveway which crossed the land in dispute and put black top and crushed stone on it[,]" and that his wife "chased people off the property[.]"[15]

The court in *Thompson* held that Gardner failed to show evidence of activities comparable to those evidenced in *Smith* and that he therefore failed to establish his claim of adverse possession.[16]

In *Roser v. Silvers*,[17] the court was faced with a traditional adverse possession claim over a driveway, but had the opportunity to address an issue of first impression in Indiana. The facts leading to the dispute are as follows. The McPeaks acquired their property from the Rosers, whose predecessors in interest were the Brickers. This property is located adjacent to and east of Silvers' lot, which Silvers obtained from her parents, the Weavers. The Weavers acquired the property in 1955, at which time the Brickers lived next door.[18]

In 1956, the Weavers installed a driveway that encroached upon the Brickers' property. The Weavers paid to have the driveway paved in 1969, and the Weavers and their successors have been using the driveway continuously since that time. The Brickers never used the driveway.[19] In 1993, the McPeaks and Silvers began feuding over the use of the driveway. Silvers filed an action to quiet title. In a bench trial, the court "quieted title in the disputed strip of property in Silvers' favor based on its determination that Silvers' parents had acquired the property by adverse possession."[20]

The Rosers and the McPeaks (hereafter the "Rosers") appealed the trial court's decision, arguing both 1) that the evidence was insufficient to support a determination that the disputed strip was acquired by adverse possession, and 2) that statements made by Silvers' late father regarding the boundary line between the properties was inadmissible hearsay.[21] The court of appeals affirmed the

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consisted "simply of having dirt thrown upon the lot from time to time to fill up holes, and also of occasionally storing lumber and wagons thereon")).

14. 134 N.E.2d 823 (Ind. App. 1956).

15. *Thompson*, 698 N.E.2d at 398-99 (quoting *Smith*, 134 N.E.2d at 827).

16. *Id.* at 399. The court rejected the Thompsons' claim on identical grounds, stating that "[b]ecause we have held above that adverse possession may not be established on these grounds, we do not address the Thompsons' claim further." *Id.*

17. 698 N.E.2d 860 (Ind. Ct. App. 1998).

18. *See id.* at 862.

19. *See id.* at 862-63.

20. *Id.* at 863.

21. *See id.* at 862. The Rosers and the McPeaks also made arguments based on an alleged violation of a separation of witnesses order and the defense of laches. *See id.*

decision of the trial court.[22]

In support of their first argument, the Rosers alleged that "the driveway had been shared by both properties in the past[,] . . . there was no fence or barrier between the properties[,] . . . the adverse possession of Silvers' predecessors was not open and notorious[,] . . . [and] there was no evidence that the Weavers ever communicated their intent to possess the property to the Brickers."[23] The court rejected these arguments, stating that they were "a mere invitation to reweigh the evidence" and that the trial court's findings were "not clearly erroneous."[24]

Next, the court analyzed a rule of evidence that previously had not been interpreted by Indiana case law, and that is particularly relevant to claims of adverse possession. At trial, the court admitted statements made by Silvers' late father pertaining to the location of the boundary line between the two properties at issue, despite a hearsay objection by the Rosers.[25] The trial court admitted the statements under Rule 803(20) of the Indiana Rules of Evidence, which provides that "[r]eputation in a community, arising before the controversy, as to boundaries of or customs affecting lands in the community . . ." are not excluded by the hearsay rule.[26]

Because no Indiana court had analyzed this rule, the court of appeals looked to other jurisdictions for interpretive guidance.[27] While courts in other jurisdictions have held that "[r]eputation evidence as to customs affecting land [are] not excluded,"[28] the court here found that the exception embodied in Rule 803(20) "applies only to reputation or general consensus evidence and does not permit the admission of specific statements or assertions made by the predecessor in interest regarding a boundary."[29] As such, the court found that it was erroneous for the trial court to permit the hearsay testimony "regarding the statements made by Silvers' late father with respect to the location of the boundary line."[30]

In *Panhandle Eastern Pipe Line Co. v. Tishner*,[31] the Indiana Court of

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22. *Id.*

23. *Id.* at 863.

24. *Id.*

25. *Id.* at 863-64.

26. *Id.* at 864 (citing IND. R. EVID. 803(20) (1998)).

27. *Id.*

28. *Id.* (citing Williams v. State, 595 So. 2d 1299, 1306 (Miss. 1992); Broyhill v. Coppage, 339 S.E.2d 32, 35 (N.C. Ct. App. 1986)).

29. *Id.* (citing Nature Conservancy v. Nakila, 671 P.2d 1025, 1033 (Haw. Ct. App. 1983); Goodover v. Lindey's Inc., 757 P.2d 1290, 1293-94 (Mont. 1988)). The court also stated that "[t]his approach comports with Indiana's common law." *Id.* (citing Ellison v. Branstrator, 54 N.E. 433, 437 (Ind. 1899) (finding no error in excluding evidence of a conversation with a surveyor regarding boundary line)).

30. *Id.* The court, however, found that the error was harmless in that it "was merely cumulative of other evidence to the effect that the western edge of the driveway marked the boundary line between the properties." *Id.*

31. 699 N.E.2d 731 (Ind. Ct. App. 1998).

Appeals addressed the elements of an adverse possession claim relative to the rights of an easement holder.[32] Panhandle operated a pipeline that traveled through Hamilton County, Indiana. The Tishners lived on real estate located in Hamilton County, which they had owned since 1956. Panhandle owned an open easement of undefined width across the Tishners' property, which provided that Panhandle had the right to "lay, maintain, operate, repair, replace, change the size of, and remove a pipeline. The Tishners [were] entitled to fully use and enjoy the premises except for the purpose granted to Panhandle."[33] In addition, the easement required that Panhandle pay for damages to crops and fences caused by the exercise of their easement rights.[34]

The Tishners built a house and driveway on the property and also made several aesthetic improvements thereto, including "the installation of a swimming pool, a patio, a brick pool wall, a pool house, a stone wall entry into the pool area, and a brick entry wall. . . . In addition, the Tishners planted several trees in proximity to [a pipeline running through the property], and some directly over the [pipeline]."[35] Panhandle did not object to the Tishners' improvements.

In 1988, Panhandle discovered problems with the pipeline that would require entry pursuant to the easement for repair of the pipeline. Panhandle explained to the Tishners that the repair work would require the removal of the brick entry wall, a portion of the stone wall, and several trees and shrubs located on the property near the pipeline.[36] In fact, the repair work required Panhandle to "remove the brick entry wall, several trees and shrubs, the stone entry wall to the pool area, and to tear up the asphalt on the Tishners' driveway."[37] Upon completion of the project, Panhandle filled in the trench and reseeded the lawn, but did not repair or replace any of the damaged improvements or landscaping.[38]

A few years after Panhandle's repair work, the Tishners began making further improvements to the property. They planted trees near the pipeline and began construction of a brick entry wall that would sit directly on top of the pipeline. Panhandle obtained a temporary restraining order to prevent the Tishners from making any further improvements that would prevent Panhandle from exercising its easement rights. Panhandle then sought a permanent injunction against the Tishners and the Tishners filed a counterclaim for damages to their improvements caused by Panhandle's work pursuant to its easement.[39] The trial court ordered Panhandle to pay damages to the Tishners, and ordered that the Tishners be allowed to erect and maintain any improvements on their

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32. The *Panhandle* decision discusses both elements of adverse possession and rights of an easement holder. The aspects of the case addressing the elements of adverse possession will be discussed here, while the portions focusing on the use of easements are discussed in Part II, *infra*.

33. *Panhandle*, 699 N.E.2d at 734.

34. *See id.*

35. *Id.*

36. *See id.* at 735.

37. *Id.*

38. *Id.*

39. *See id.*

property that existed prior to the repair work described above. The court ruled, however, that the Tishners could not make improvements or erect structures that fall within the area that Panhandle claims as an easement.[40]

The first issue addressed by the court on appeal was whether Panhandle's easement was partially extinguished by the Tishners' adverse possession of the portion of the property subject to the easement. In holding that the easement was not partially extinguished, the court discussed two elements of an adverse possession claim, namely, that the claimant's use is "hostile" and that such use is "exclusive."[41] The court found that neither element was satisfied.

The court began its analysis by recognizing that "[a]n easement may be extinguished by adverse possession."[42] However, the court found that the Tishners failed to establish that their use of Panhandle's easement was "hostile."[43] According to the court, possession will be considered "hostile" if "the party claiming adverse use does not disavow his or her right to possess the property or acknowledge that it is subservient to the title of the true owner."[44] Here, the Tishners made no attempt to exclude Panhandle from its easement after Panhandle received a temporary restraining order prohibiting the Tishners from interfering with Panhandle's work. Therefore, the court concluded that "[t]here was no sustained hostile use of the easement."[45]

Further, the court found that the Tishners "failed to establish that their use of the easement was exclusive."[46] This element of an adverse possession claim requires that the party "claims possession adversely *to the exclusion of all others*" and requires possession "of such a nature that it operates as an ouster of the owner."[47] Panhandle's continuous use of the easement throughout the relevant time period negated any claims of "ouster" made by the Tishners. Panhandle regularly conducted projects on the property, performed aerial surveillance, conducted annual foot patrols, and even sought injunctive relief when the Tishners attempted to interfere with its access to the property.[48] The court thus concluded that "[t]o the extent that the trial court used the doctrine of adverse possession as the basis for its decision, it is unsupported by the evidence . . . ."[49]

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40. *Id.*
41. *Id.* at 736-37.
42. *Id.* at 736 (citing McKinney v. Lanning, 38 N.E. 601, 603 (Ind. 1894)).
43. *Id.*
44. *Id.* (citing Kline v. Kramer, 386 N.E.2d 982, 988 (Ind. Ct. App. 1979)).
45. *Id.* at 737.
46. *Id.*
47. *Id.* (emphasis added) (citing Herrell v. Casey, 609 N.E.2d 1145, 1148 (Ind. Ct. App. 1993); Davis v. Sponhauer, 574 N.E.2d 292, 298 (Ind. Ct. App. 1991)).
48. *See id.*
49. *Id.*

II. EASEMENTS

A. Scope and Use of Easements

In addition to addressing certain elements of an adverse possession claim as they relate to extinguishing an easement, the court in *Panhandle* had the opportunity to clarify the status of Indiana law with regard to the scope of an easement and the parameters of an easement holder's permissible use of an easement.[50]

1. Easement Implied to Ensure Compliance with Federal Law.—The court in *Panhandle* noted that Panhandle's operation of the pipeline running through the Tishners' property was governed by the Natural Gas Pipeline Safety Act,[51] which sets forth the "minimum federal safety standards for the design, installation, inspection, emergency procedures, testing, extension, construction, operation, replacement, and maintenance of pipeline facilities."[52] The court continued by stating that "where common law rules of property are inconsistent with the congressional scheme set forth in the Act, the common law rules must give way, rendering any property use inconsistent with the Act subject to injunction."[53] As the court then recognized, it follows logically that "[a]n easement which grants the right to operate a natural gas pipeline must, if the easement is not to be wholly illusory, imply the right to operate the pipeline in accordance with applicable federal law."[54] Because federal law requires Panhandle to inspect the pipeline at regular intervals, as well as implement other safety measures, the right to access to the property for the purpose of complying with the federal law requirements is implied. The court concluded that Panhandle retained all of its rights to the easement.[55]

2. Permissible Use of Dominant and Servient Estates.—The Tishners argued that Panhandle owed them a duty to take reasonable steps to protect the improvements placed by the Tishners near the pipeline. The trial court agreed, awarding damages for repair of the Tishners' pool wall, patio, yard, curb, driveway, and playground.[56] In addressing the propriety of the damages award, the court of appeals examined the scope of Panhandle's easement.

The court noted that the terms of the grant creating the easement indicated that the easement was an "open easement" of undefined width.[57] As such, the

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50. *See id.* at 737-39. The facts of the *Panhandle* decision are set out in their entirety in Part I. *See supra* notes 31-49 and accompanying text.

51. *Id.* at 737 (citing 49 U.S.C.A. app. §§ 1671-88 (1994) (recodified at 49 U.S.C. §§ 60101-25 (1994 & Supp. II 1996 & Supp. III 1997)).

52. *Id.*

53. *Id.* at 738 (citing Swango Homes, Inc. v. Columbia Gas Transmission Corp., 806 F. Supp. 180, 184 n.2 (S.D. Ohio 1992)).

54. *Id.*

55. *Id.*

56. *Id.*

57. *Id.*

easement covered only "the area reasonably necessary to carry out the purposes of the easement."[58] It was the court's duty then to determine the extent of the easement given the particular necessities at hand.[59]

At trial, Panhandle demonstrated that an easement sixty-six feet wide would be sufficient for the purpose of maintaining and repairing the pipeline.[60] The Tishners provided no contradictory evidence. Further, the court noted that easements of sixty-six feet had received prior judicial approval for pipelines operated by Panhandle in the same area.[61] An easement of sixty-six feet was thus deemed reasonable.[62]

The court also addressed the respective rights of the owners of both the dominant and servient estates. Within an easement, the owner of the easement, or the dominant estate, possesses all the rights "necessarily incident to the enjoyment of the easement."[63] The owner of the easement "may make repairs, improvements, or alterations that are reasonably necessary to make the grant of the easement effectual."[64] The owner of the servient estate, on the other hand, may use the property that is subject to the easement "in any manner and for any purpose consistent with the enjoyment of the easement, and the dominant estate cannot interfere with the use."[65] The servient estate owner "may not so use his land as to obstruct the easement or interfere with the enjoyment thereof by the owner of the dominant estate."[66]

Based on the foregoing statements of law, the court in *Panhandle* concluded that Panhandle had the right to enter the Tishners' property for the purpose of making repairs and replacements to the pipeline, "including any necessary excavation, without regard to structures erected upon the easement, and the Tishners erected such structures at their peril."[67] Because the express terms of the easement grant made Panhandle liable only for damages to crops and fences within the easement, the court held that Panhandle's liability in this case was limited to such.[68] The court remanded the case for a determination of whether

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58. *Id.*

59. *See id.* (citing Rees v. Panhandle E. Pipe Line Co., 452 N.E.2d 405, 410 (Ind. Ct. App. 1983)).

60. *See id.*

61. *Id.* at 738-39 (citing *Rees*, 452 N.E.2d at 405; Rees v. Panhandle E. Pipe Line Co., 377 N.E.2d 640 (1978)).

62. *Id.*

63. *Id.* at 739 (citing Litzelswope v. Mitchell, 451 N.E.2d 366, 369 (Ind. Ct. App. 1983)).

64. *Id.*

65. *Id.* (citing Holding v. Indiana & Mich. Elec. Co., 400 N.E.2d 1154, 1157 (Ind. Ct. App. 1980)).

66. *Id.*

67. *Id.*

68. *Id.* The court distinguished Panhandle's duties "within" the easement from its duties "outside" the easement. Outside the easement

> a landowner has an absolute right to have his land in its natural state laterally supported by the lands of adjoining landowners. If the adjoining landowner excavates on his land

the damaged structures were within the area of the property subjected to the easement and for a determination of damages.[69]

B. Prescriptive Easements and Disclaimer Thereof

To acquire an easement by prescription, a claimant must show "actual, hostile, open, notorious, continuous, uninterrupted, adverse use for a period of twenty years under a claim of right or by continuous adverse use with knowledge and acquiescence of the owner of the servient estate."[70] In *Book v. Hester*,[71] the court of appeals addressed the enforceability of a disclaimer of interest in a prescriptive easement.

The Books raised cattle on a forty-acre parcel of property. The property could be accessed only via a gravel road crossing Hester's property, which was located to the east of the Books' property. The road had been used continuously for access to the forty acres since at least 1907. In October 1995, Hester erected a fence blocking the Books' use of the road. The Books then sought injunctive and declaratory relief, claiming that they had acquired a prescriptive easement for use of the road.[72] Hester argued that the Books had relinquished any right to use of the road that they might have acquired when they signed a disclaimer of

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> thereby depriving the lands of his neighbor of lateral support, the adjoining landowner is absolutely liable for such damage even if he is free from negligence.

Id. The court therefore held that Panhandle had an absolute duty to provide lateral support to the Tishners' land. However, the court recognized that "liability for damage to buildings resulting from the loss of lateral support must be based upon the negligence of the adjoining landowner in carrying on the activity which occasioned the loss of lateral support." *Id.* Panhandle, then, had a duty to use reasonable care to avoid the negligent removal of lateral support to the improvements erected on the property by the Tishners.

69. *Id.* During the survey period, the Indiana Court of Appeals also had the opportunity to address easement issues in the context of riparian rights. *See* Abbs v. Town of Syracuse, 686 N.E.2d 928, 928-32 (Ind. Ct. App. 1997). In *Abbs*, shoreline property owners sued the Town of Syracuse and various residents for erecting piers and docking boats at the ends of certain public streets and alleys which lead to water's edge. The Indiana Court of Appeals affirmed the lower court's ruling that "in creating the public right-of-way, the grantors intended to grant to the public riparian rights of access to the lake, including the right to establish and use piers, subject only to regulation by the proper municipal or governmental authority." *Id.* at 929.

70. Walter Krieger, *1993 Developments in Indiana Property Law*, 27 IND. L. REV. 1285, 1287 (1994) (citing IND. CODE § 32-5-1-1 (1979) (recodified at IND. CODE § 32-5-1-1 (1998)); Greenco, Inc. v. May, 506 N.E.2d 42, 45 (Ind. Ct. App. 1987); Searcy v. LaGrottee, 372 N.E.2d 755, 757 (Ind. Ct. App. 1978)). *See also* CUNNINGHAM ET AL., *supra* note 2, at 451 (noting that the elements required to establish a prescriptive easement are nearly identical to those required to establish adverse possession, with the chief distinction being that "in adverse possession the claimant occupies or possesses the disseisee's land, whereas in prescription he makes some easement-like use of it").

71. 695 N.E.2d 597 (Ind. Ct. App. 1998).

72. *See id.* at 598.

interest in 1989 relating to a quiet title action brought by the Swopes, the predecessors in interest to Hester.[73] The Books countered that the 1989 disclaimer was unenforceable because it was not recorded pursuant to section 32-3-2-7 of the Indiana Code.[74]

Section 32-3-2-7 of the Indiana Code provides, in relevant part, that "[a] disclaimer of an interest in real property is effective . . . *only if it is recorded in each county where the real property is located*."[75] In rejecting the Books' argument pursuant to this section, the court analyzed the Probate Code Study Commission Introductory Comments ("the Comments") to the disclaimer statute.[76] The Comments provide that a "disclaimer is a refusal to accept property *ab initio* . . . ."[77] The Comments further state that the "law of disclaimer is founded on the property law concept that *a transfer of title to property is not complete until it is accepted by the recipient and that no person can be forced to accept property against his will*."[78] Finally, the court noted that the disclaimer statute itself reads that the "right to disclaim an interest . . . is barred by acceptance of the interest . . . ."[79]

Based on the above commentary, the court concluded that "the disclaimer statute only contemplates the disclaimer of an interest in property *prior to* acceptance . . . [and that] [a]s such, the statute does not apply to the present case."[80] In this case, the Books acquired their property by contract in 1969, at which time they accepted title without disclaiming their interest in the easement. The court stated that "[h]aving had the use and benefit of the easement for many years, the Books cannot now claim relief under a statute which, if it applied, would require them to disclaim their interest *ab initio*."[81] Because the disclaimer statute did not apply, the Books could not rely upon it to require that for their disclaimer to be enforceable, it must have been previously recorded.

As an alternate ground for its decision, the court stated that "[e]ven if the disclaimer statute did apply, the Books had actual notice of the disclaimer and, thus, cannot now complain that they were prejudiced by the fact that the

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73. *See id.* at 598-99 & n.3.

74. *See id.* at 599.

75. *Id.* at 600 (quoting IND. CODE § 32-3-2-7 (1993) (emphasis added) (recodified at IND. CODE § 32-3-2-7 (1998)). Indiana's disclaimer statute is located at sections 32-3-2-1 to 32-3-2-15 of the Indiana Code and outlines the procedures necessary to disclaim certain property interests. *See id.* (enumerating the types of property interests to which the disclaimer statute is applicable).

76. *Id.* (citing section 32-3-2-14 of the Indiana Code, which provides that commission's comments may be consulted by the court in applying the disclaimer statute (recodified at IND. CODE § 32-3-2-14 (1998)).

77. *Id.* (quoting IND. CODE § 32-3-2-14 (1993) (recodified at IND. CODE § 32-3-2-14 (1998)) (Probate Code Study Comm'n Introductory Cmts.) (emphasis added)).

78. *Id.* (emphasis added).

79. *Id.* (quoting IND. CODE § 32-3-2-11 (1993) (recodified at IND. CODE § 32-3-2-11 (1998)).

80. *Id.* (emphasis added).

81. *Id.*

disclaimer was not recorded."[82] The court noted that "the disclaimer statute is designed to give constructive notice to third-parties[83] . . . [and that] [a]s a general rule, a party to a deed, mortgage or other instrument concerning an interest in real estate is bound by the instrument whether or not it is recorded."[84] Thus, the Books could not rely on technical compliance with the disclaimer statute to render their disclaimer of the prescriptive easement unenforceable.

In rendering its decision in *Book*, the court distinguished the holding from *Popp v. Hardy*,[85] that "a quiet title decree was not res judicata against a party not joined in the quiet title action."[86] The Books relied on this case in arguing that the disclaimer should not be enforced, as they were not specifically named in the 1989 quiet title action brought by the Swopes, in connection with which the disclaimer was executed.[87] In distinguishing *Popp* from the present case, the court noted that "the Books voluntarily relinquished their interest in the easement. With the disclaimer in hand, the Swopes had no reason to make the prescriptive easement an issue and join the Books, who had denied having any claim or interest in the property."[88] In addition, the court noted that Hester did not argue that the Books' lawsuit was barred by the Swopes' quiet title decree, but rather that it is barred "by virtue of their disclaimer."[89] Therefore, the court found *Popp* distinguishable and affirmed the trial court's ruling against the Books.[90]

III. EMINENT DOMAIN

The acquisition of land by eminent domain is governed in Indiana by statute.[91] Any objection by a landowner to the appropriation and condemnation of land by eminent domain must be made in the manner specified by the statute. Section 32-11-1-5 of the Indiana Code provides the following:

> Any defendant may object to such proceedings on the grounds that the court has no jurisdiction either of the subject-matter or of the person, or that the plaintiff has no right to exercise the power of eminent domain for the use sought, or for any other reason disclosed in the complaint or set up in such objections. Such objections shall be in writing, separately stated and numbered, and shall be filed not later than the first appearance of such defendant; and no pleadings other than the complaint and such statement or objections shall be allowed in such cause, except the answer

82. *Id.*
83. *Id.* (citing McIntyre v. Baker, 660 N.E.2d 348, 352 (Ind. Ct. App. 1996)).
84. *Id.* (citing Blair v. Whitaker, 69 N.E. 182 (Ind. App. 1903)).
85. 508 N.E.2d 1282 (Ind. Ct. App. 1987).
86. *Book*, 695 N.E.2d at 601 (citing *Popp*, 508 N.E.2d at 1287).
87. *See id.*
88. *Id.*
89. *Id.*
90. *Id.*
91. IND. CODE §§ 32-11-1-1- to -13 (1998).

provided for in section 8 of this chapter: provided, that amendments to pleadings may be made upon leave of court.[92]

In *Maharis v. Orange County*,[93] the Indiana Court of Appeals demonstrated the harsh effects of the above statutory provision resulting from a failure to strictly comply with the provision's terms. Orange County filed a complaint for Appropriation of Real Estate against Maharis in an effort to obtain a portion of Maharis' land for a bridge improvement project. A summons and notice was issued to Maharis on May 10, 1995.[94] Maharis failed to respond to the summons and an Order of Appropriation and Appointment of Appraisers was entered on June 5, 1995.[95] The Order, however, was set aside on June 8, 1995, because the May summons and notice were returned unclaimed.[96] Because all previous attempts to serve the summons and notice were unsuccessful, Summons by Publication was issued on July 13, 1995, which required a response by August 31, 1995.[97] Two days before the deadline, Maharis' attorney filed an appearance and moved for an extension of time to respond. This motion was denied and an Order of Appropriation of Real Estate and Appointment of Appraiser was entered on September 1, 1995.[98]

On October 10, 1995, Maharis filed an answer to the complaint that included numerous affirmative defenses, a counterclaim against Orange County, and a demand for trial by jury. On October 26, 1995, Orange County filed a motion to strike all of Maharis' filings because they were not filed in accordance with the provisions of the condemnation statute. The trial court granted the motion to strike.[99]

In affirming the trial courts' decision, the court of appeals explained that the acquisition of land via eminent domain is governed by statute and that "all objections to the appropriation and condemnation of land . . . must be filed 'not later than the first appearance of such defendant.'"[100] The court explained that Maharis' objections should have been filed with the appearance, but were incorrectly filed in other pleadings.[101] Thus, the court found that "Maharis [had] not preserved any error for appeal on [the] issues" and that the "trial court did not err in striking Maharis' pleadings that were not allowed under the eminent domain statute."[102]

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92. *Id.* § 32-11-1-5.
93. 685 N.E.2d 1131 (Ind. Ct. App. 1997).
94. *See id.* at 1132.
95. *See id.*
96. *See id.*
97. *See id.*
98. *See id.*
99. *See id.* at 1132-33.
100. *Id.* (quoting IND. CODE § 32-11-1-5 (1993) (recodified at IND. CODE § 32-11-1-5 (1998))).
101. *Id.*
102. *Id.*

In *Lehnen v. State*,[103] the court of appeals highlighted the time limits for filing exceptions to a report of appraisal and the "due process" requirements of an eminent domain proceeding. The State of Indiana filed a complaint for appropriation of a portion of Leynen's real estate for the purpose of improvements to U.S. Route 231. The lower court appointed three appraisers to assess the damages that would be sustained by the landowner.[104] The report set damages at $129,984. Lehnen and the State of Indiana, however, filed exceptions to the report.[105]

On September 27, 1995, the State of Indiana filed a second amended complaint, which reflected changes in the construction plans for the highway. The trial court appointed three appraisers to assess the damages sustained by the landowner.[106] Damages were assessed in a new report at $166,000. Lehnen filed no exceptions to the report. Based on the absence of exceptions, judgment was entered on behalf of the landowner in the amount of $166,000.[107] On June 3, 1996, Lehnen filed a motion to vacate the judgment, alleging mistake, surprise and excusable neglect for failure to file exceptions to the appraisal report. The motion was denied.[108]

In affirming the lower court's decision, the Indiana Court of Appeals stated that in regard to a report of appraisal, either or both parties may file exceptions to the appraisal within twenty days of the report of appraisal being filed.[109] "Compliance with all the provisions relating to the assessment of damages and their recovery is essential."[110] The court explained that the landowner considered the filing of exceptions unnecessary regarding the second report because exceptions were filed regarding the initial report of appraisal.[111] However, the court stated that "[s]hould a new appraisement be granted by the court . . . it will be open to the same proceedings as a first one would be."[112] Thus, the landowner was required, by statute,[113] to file exceptions to the second appraisal report within

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103. 693 N.E.2d 580 (Ind. Ct. App. 1998).

104. *See id.* at 581.

105. *See id.*

106. *See id.*

107. *See id.*

108. *See id.*

109. *Id.* at 582. Indiana Code section 32-11-1-8 states:

> Any party to such action, aggrieved by the assessment of benefits or damages, may file written exceptions thereto in the office of the clerk of such court in vacation, or in open court if in session, within twenty (20) days after the filing of such report, and the cause shall further proceed to issue, trial and judgment as in civil actions; the court may make such further orders, and render such findings and judgments as may seem just.

IND. CODE § 32-11-1-8 (1993) (recodified at IND. CODE § 32-11-1-8 (1998)).

110. *Lehnen*, 693 N.E.2d at 582.

111. *Id.*

112. *Id.* (citing Swinney v. Fort Wayne & Cincinnati Ry. Co., 59 Ind. 205, 218 (1877)).

113. IND. CODE § 32-11-1-8 (1993) (recodified at IND. CODE § 32-11-1-8)).

twenty days of the report being filed.[114] The court concluded that because neither party filed exceptions, the trial court did not abuse its discretion in approving the appraisal report.[115]

The landowner further argued that he was denied his "due process" rights because the report failed to inform him of his statutory right to file exceptions within the twenty day time period. He argued that his constitutional rights of notice were not met because the report is to be treated as a complaint, and as such, must provide adequate notice.[116]

The court disagreed with the landowner's contentions. The court stated that in the context of an eminent domain proceeding, the report and the exceptions serve to establish that only the issue of damages is to be tried.[117] The court concluded that "the report of the appraisers is not a complaint for purposes of notice to the landowners and that Lehnen received adequate notice of the proceedings to satisfy due process."[118]

The Indiana Court of Appeals further addressed issues relating to appraisal reports in *Daugherty v. State*.[119] On March 16, 1995, the State of Indiana commenced an eminent domain action against Daugherty for real estate located in Knox County. The State offered Daugherty $1300 for the property. After the landowner rejected the State's offer, the State filed a complaint for appropriation of real estate.[120]

The lower court entered an order of appropriation and appointment of appraisers.[121] The appraisers filed their report, which appraised the damage to the landowner at $4500. The State filed exceptions to the report based on the following: "[The report] overstated the damages to the residue of Daugherty's property, understated the value of the benefits to the residue, and overstated the amount of just compensation due to Daugherty."[122]

On April 18, 1997, the State withdrew its exceptions and moved for an entry of judgment. Because the landowner had not entered any exceptions, the lower court granted the State's Motion for Judgment and ordered the State to pay $4500 to Daugherty.[123]

The sole issue on appeal was whether the trial court erred in permitting the State of Indiana to unilaterally withdraw its exceptions to the appraisal report.[124] In affirming the lower court's decision, the Indiana Court of Appeals analyzed

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114. *See Lehnen*, 693 N.E.2d at 582.

115. *Id.*

116. *See* Best Realty Corp. v. State, 400 N.E.2d 1204, 1206 (Ind. Ct. App. 1980).

117. *Lehnen*, 693 N.E.2d at 582.

118. *Id.*

119. 699 N.E.2d 780 (Ind. Ct. App. 1998).

120. *See id.* at 781.

121. *See id.*

122. *Id.*

123. *See id.*

124. *Id.*

Indiana case law regarding the issue.[125] The court noted that an exception had been established to the general rule that stated that by dismissing his own exceptions, a party may preclude others from litigating.[126] In *State v. Blount*, the court found that "it is unnecessary that a land-owner file exceptions as a condition precedent to his right to recovery, if exceptions have been filed by the condemning party."[127] In making this decision, "the trial court noted that Blount had invested both significant time and effort in preparing for trial and it would have been unfair to allow one party to unilaterally withdraw its exceptions."[128]

After reviewing *Blount* and subsequent decisions, the court concluded that: "a party does not have an absolute right to withdraw exceptions to the appraisers' report; rather, the withdrawal of exceptions is subject to the trial court's discretion."[129] Based on the facts of the instant case, the court concluded that the trial court did not abuse its discretion in allowing the withdrawal and that the lower court properly granted the State's motion for judgment.[130]

In *Jenkins v. Board of County Commissioners*,[131] the court of appeals was faced with an inverse condemnation proceeding. In this case, a roadway was altered to eliminate a double T-intersection thereby allowing traffic to proceed straight on the roadway without the necessity of making a turn.[132] Utilizing the power of eminent domain, the Board of County Commissioners of Madison County (the "Board") acquired property from the Appellant-Plaintiff's neighbor to accomplish the project.[133] After the construction was complete, approximately 675 feet of the roadway was no longer adjacent to the Appellant-Plaintiff's property.[134] The Appellant-Plaintiff filed a Complaint for Inverse Condemnation claiming a loss of ingress and egress, road frontage, and corner influence.[135] The lower court ruled in favor of the Board. In ruling for the Board, the lower court concluded that 1) "the removal of the road bed represented a seventeen percent (17%) loss of total road frontage[,]" 2) "there was no substantial and material

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125. *Id.* at 782.

126. *Id.* (citing State v. Blount, 290 N.E.2d 480 (Ind. App. 1972)).

127. *Blount*, 290 N.E.2d at 483-84.

128. *Daugherty*, 699 N.E.2d at 782 (citing *Blount*, 290 N.E.2d at 483).

129. *Id.* The court explained that the factors to be used in the determination include:

> [T]he length of time between the filing of the appraisers' report and the motion to withdraw, whether the withdrawing party is attempting to do so on the eve of the trial, whether the withdrawing party and trial court have been put on notice of the other party's dissatisfaction with the report, either that be through the filing of belated exceptions or otherwise, and the extent of trial preparation which has already occurred, including the securing of expert witnesses and the extent of discovery.

Id. at 783.

130. *Id.*

131. 698 N.E.2d 1268 (Ind. Ct. App. 1998).

132. *Id.* at 1270.

133. *Id.*

134. *Id.*

135. *Id.*

interference with Jenkins' rights of ingress and egress[,]" and 3) there was no 'compensable taking.'"[136]

The issue on appeal was whether the trial court erred in determining that the Appellant-Plaintiff's property had not been "taken."[137] In affirming the lower court's decision, the court explained that "[i]t has long been recognized that the right of ingress and egress is a property right which cannot be taken without compensation."[138] A "taking" of property includes "any substantial interference with private property which destroys or impairs one's free use and enjoyment of the property or one's interest in the property."[139] The trier of fact, the court explained, resolves the question of whether the interference is substantial.[140]

The court determined that the evidence supported the trial court's decision. The court explained that "[a]t most the record demonstrates that [the Appellant-Plaintiff] was inconvenienced in obtaining access to his property. . . . A property owner is not entitled to unlimited access to abutting property at all points along the highway."[141] In addition, the court stated that the "fact that ingress and egress is made more circuitous and difficult does not itself constitute a taking of private property."[142] The court concluded by stating that "[w]here, as here, there has been no taking the question is whether the action of the governmental entity diminished the value of the property in its present use. . . . There is no evidence that as farmland the value of [the Appellant-Plaintiff's] property has been reduced by reason of the relocation of [the roadway]."[143]

IV. Landlord and Tenant

A. Security Deposits Statute

When drafting the Indiana Security Deposits Statute,[144] the Legislature confined the purposes for which a landlord may use a security deposit to the following:

> (1) To reimburse the landlord for actual damages to the rental unit or any ancillary facility that are not the result of ordinary wear and tear expected in the normal course of habitation of a dwelling.
> (2) To pay the landlord for all rent in arrearage under the under the rental agreement, and rent due for premature termination of the rental agreement by the tenant.

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136. *Id.*
137. *Id.*
138. *Id.*
139. *Id.* (citing Board of Comm'rs v. Joeckel, 407 N.E.2d 274, 278 (Ind. Ct. App. 1980)).
140. *Id.*
141. *Id.* at 1271 (citing State v. Ensley, 164 N.E.2d 342, 348 (Ind. 1960)).
142. *Id.*
143. *Id.* at 1271-72.
144. IND. CODE §§ 32-7-5-1 to -19 (1993) (recodified at IND. CODE §§ 32-7-5-1 to -19 (1998)).

> (3) To pay for the last payment period of a residential rental agreement where there is a written agreement between the landlord and the tenant that stipulates the security deposit will serve as the last payment of rent due.
> (4) To reimburse the landlord for utility or sewer charges paid by the landlord that:
> (A) are the obligation of the tenant under the rental agreement; and
> (B) are unpaid by the tenant.[145]

The Legislature also provided a notice requirement within the statute that states:

> In case of damage to the rental unit or other obligation against the security deposit, the landlord shall mail to the tenant, within forty-five (45) days after the termination of occupancy, an itemized list of damages claimed for which the security deposit may be used as provided in section 13 of this chapter, including the estimated cost of repair for each damaged item and the amounts and lease on which the landlord intends to assess the tenant. The list must be accompanied by a check or money order for the difference between the damages claimed and the amount of the security deposit held by the landlord.[146]

During the survey period, three cases were decided by the Indiana Court of Appeals highlighting various provisions of the Indiana Security Deposits Statute, particularly the above limited purposes provision and notice requirement. In *Deckard Realty & Development v. Lykins*,[147] a landlord brought an action against four tenants for unpaid rent and damages to a house.[148] The tenants, students at Indiana University, entered a one-year lease and secured the lease with an $850 deposit.[149] Upon application for the lease, the landlord's agent wrote down the address of one of the tenants and placed the address in the rental file.[150] Later, after an inspection in which the landlord discovered that marijuana was being grown throughout the house, the landlord requested that the tenants vacate the premises immediately.[151]

The sole issue presented to the court of appeals for review was whether the landlord's knowledge of one of the four tenant's addresses was adequate notice of the tenants' forwarding address as required by the Indiana Security Deposits Statute.[152] In addressing the landlord's liability under the statute, the court of

145. *Id.* § 32-7-5-13.
146. *Id.* § 32-7-5-14.
147. 688 N.E.2d 1319 (Ind. Ct. App. 1997).
148. *See id.*
149. *See id.* at 1320.
150. *See id.*
151. *See id.* at 1320-21.
152. *Id.* at 1321. The statute provides the following: "The landlord is not liable under this chapter until supplied by the tenant in writing with a mailing address to which to deliver the notice

appeals stated that "a tenant must show that he provided the landlord with a written record of an address, which was intended to be his forwarding address."[153] If an address is provided, the landlord is required to provide to the tenants an itemized list of damages within forty-five days of the termination of the tenants' occupancy.[154] Failure to do so "constitutes an agreement by the landlord that no damages are due."[155] The court of appeals concluded that three of the tenants had not supplied the landlord with their forwarding address and that a material issue of fact remained as to whether the one address supplied to the landlord was intended to be the fourth tenant's forwarding address.[156]

In *Greasel v. Troy*,[157] the Indiana Court of Appeals addressed the statutory notice requirement of the Indiana Security Deposits Statute.[158] In *Greasel*, after the tenant had vacated the premise at the lease expiration, the landlord performed an inspection of the house and detected a strong pet odor that necessitated replacement of the carpet.[159] As required by statute, the landlord provided the tenant with an itemized statement of damages that included a listing for the estimated cost of carpet replacement.[160] The tenant filed suit in small claims court for return of the security deposit. The landlord filed a counterclaim for damages plus costs, interest, and attorney fees.[161] On September 30, 1996, the lower court entered judgment in the landlord's favor for which the landlord received the $1000 security deposit, $400 in damages, and $700 in attorney fees.[162]

In *Greasel*, the dispute centered on whether the landlord complied with the statutory notice requirement of the Indiana Security Deposit Statute. In her statement of damages, the landlord listed the carpet damage from the pet odor, as well as other items that she did not consider acceptable.[163] The other items listed, however, were not assigned an estimated cost.[164] In deciding that the notice was sufficient, the court stated that the "purpose of the notice provision is to inform the tenant that the landlord is keeping the security deposit and for

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and amount prescribed by this subsection." IND. CODE § 32-7-5-12(a)(1993) (recodified at IND. CODE § 32-7-5-12(a) (1998)).

153. *Deckard Realty & Dev.*, 688 N.E.2d at 1322. The court further noted that a "landlord is not liable for failing to itemize its damages until the tenant has supplied the landlord with an address to deliver the required notice." *Id.* at 1322 n.3.

154. *See id.* at 1321 (citing IND. CODE § 32-7-5-12(a)(3) & (14)).

155. *Id.* (citing IND. CODE § 32-7-5-15 (1993) (recodified at IND. CODE § 32-7-5-15 (1998)).

156. *Id.* at 1322.

157. 690 N.E.2d 298 (Ind. Ct. App. 1997).

158. *See* IND. CODE § 32-7-5-14 (1993) (recodified at IND. CODE § 22-7-5-14 (1998)).

159. *See id.* at 301.

160. *See id.*

161. *See id.*

162. *See id.*

163. *See id.* at 302.

164. *See id.*

what reason."[165] The court further stated that such notice gives the tenant the opportunity to challenge the costs for which the deposit was used by the landlord.[166] The court noted that the landlord's failure to assign cost estimates to the other items did not render the statement insufficient under the statute because she made no claim for damages other than the carpet at trial.[167] If provided for in the lease agreement, "other items" may even include attorney fees.[168]

In *Pinnacle Properties v. Saulka*,[169] tenants filed a complaint seeking the return of their $2500 security deposit.[170] The trial court entered judgment in favor of the tenants.[171] On appeal, the first issue involved whether security deposits could be used by landlords for certain purposes.[172] As highlighted above, security deposits may only be used by landlords for limited purposes.[173] The landlord's damage report sent to the tenants listed the following charges against the tenant's security deposit: 1) cleaning/trash out, $558; 2) carpet cleaning, $180.40; 3) carpet replacement, $550; 4) painting, $700; 5) other damages, $670; 6) unpaid rent, $330.64.[174]

In deciding that the itemized list was not in compliance with the statute, the court stated that "the Security Deposits Statute . . . must be strictly construed."[175] The court stated that a landlord "cannot merely itemize and include the estimated cost of repair for some items and then arbitrarily lump together 'other damages' leaving the tenant unable to discern for what purpose his security deposit is being retained and whether such charge is proper or reasonable."[176] The court concluded that the landlord's failure to comply with the notice provision "constitutes an agreement that no damages are due."[177] The tenants were refunded their security deposit and were awarded attorney fees pursuant to the statute.[178]

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165. *Id.* (citing Meyers v. Langley, 638 N.E.2d 875, 878 (Ind. Ct. App. 1994)).

166. *Id.*

167. *Id.* In fact, the court noted that the landlord's compliance with the statutory notice requirement "preserves her right to recover 'other damages' beyond the amount of the security deposit to which she is entitled." *Id.* (quoting Miller v. Geels, 643 N.E.2d 922, 925 (Ind. Ct. App. 1994)).

168. Section 32-7-5-12-(c) of the Indiana Code provides that "[t]his section does not preclude the landlord or tenant from recovering other damages to which either is entitled." IND. CODE § 32-7-5-12(c) (1993) (recodified at IND. CODE § 32-7-5-12(c) (1998)).

169. 693 N.E.2d 101 (Ind. Ct. App. 1998).

170. *Id.* at 103.

171. *See id.*

172. *Id.*

173. *See* IND. CODE § 32-7-5-13 (1998).

174. *See Pinnacle Properties*, 693 N.E.2d at 104.

175. *Id.* (citing Miller v. Geels, 643 N.E.2d 922, 927 (Ind. Ct. App. 1994)).

176. *Id.*

177. *Id. See* IND. CODE § 32-7-5-15 (1998).

178. The Indiana statute provides the following in regard to attorney fees:

B. Landlord Duty of Care

Under traditional Indiana law, a landlord covenants to a tenant to 1) deliver possession of the premises on the first day of the lease, 2) not interfere with the tenant's quiet enjoyment of the premises, and 3) provide habitable premises.[179] The Indiana Court of Appeals in *Smith v. Standard Life Insurance Co. of Indiana*,[180] addressed various aspects of a landlord's duty of care owed to a tenant. In *Smith*, an employee slipped and fell on an icy sidewalk outside of her place of employment. The employee filed a complaint for negligence against the owner and lessor of the premises.[181] The lower court entered summary judgment for the owner and lessor of the premises.[182]

The primary issue on appeal was whether an employee of a tenant qualifies as a "third person" under the public use exception to the general rule of non-liability for landlords.[183] In deciding that the lower court did not err in granting summary judgment for the landlord, the court addressed whether the landlord had a duty to the employee of the tenant under either the general rule of non-liability for landlords or the public use exception.[184]

Under the general rule of non-liability for landlords, the law is settled regarding a landlord's duty of reasonable care. The landlord's duty can be stated

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> A landlord who fails to provide a written statement within forty-five (45) days of termination of the tenancy or the return of the appropriate security deposit is liable to the tenant in an amount equal to the part of the deposit withheld by the landlord, plus reasonable attorney's fees and court costs.

IND. CODE § 32-7-5-16 (1998).

179. *See generally* Avery v. Dougherty, 2 N.E.2d 123 (Ind. 1985); Kostuck v. Vincent D., 684 N.E.2d 573 (Ind. Ct. App. 1997); Voss v. Capital City Brewing Co., 96 N.E. 11 (Ind. App. 1911). In *Bradtmiller v. Hughes Properties, Inc.*, 693 N.E.2d 85 (Ind. Ct. App. 1998), a tenant sued a landlord for negligence after being attacked and assaulted in the apartment building parking lot. In deciding that the landlord did not have a duty to protect the tenant, the court explained that "the mere relationship of landlord and tenant did not impose upon [the landlord] a legal duty to protect [the tenant] against the intentional criminal acts of unknown third parties. Foreseeability of the type of harm is required and, here, criminal activity was not a reasonably foreseeable risk." *Id.* at 90.

180. 687 N.E.2d 214 (Ind. Ct. App. 1997).

181. *See id.* at 216.

182. *See id.*

183. *Id.*

184. *Id.* at 217-19. The public use exception was explained as follows:

> Where premises are leased for public or semi-public purposes, and at [the] time of lease[,] conditions exist which render premises unsafe for purposes intended, or constitute a nuisance, and landlord knows or by exercise of reasonable care ought to know of conditions, and a third person suffers injury on account thereof, landlord is liable, because [the] third person is there at invitation of landlord, as well as of tenant.

Id. at 217 (quoting Walker v. Ellis, 129 N.E.2d 65, 73 (Ind. App. 1955)).

as follows:

> [A]s a general rule, in the absence of statute, covenant, fraud or concealment, a landlord who gives a tenant full control and possession of the leased property will not be liable for personal injuries sustained by the tenant or other persons lawfully upon the leased property. Generally, once possession and control of property have been surrendered, a landlord does not owe a duty to protect tenants from defective conditions.[185]

In *Smith*, the landlord had relinquished complete possession and control of the premises in favor of the tenant. The tenant was responsible for the maintenance and repair of the premises, and employees of the tenant removed the snow and ice from the sidewalks. Based on these facts, the court determined that under the aforementioned general rule, the landlord did not owe the tenant's employee any type of duty.[186]

In order for the public use exception to apply, the court of appeals explained that the employee must provide evidence to support the following:

> (1) the property was leased for a public purpose, (2) a condition existed at the time of the lease which rendered the premises unsafe and the landlord knew or should have known of the condition by the exercise of reasonable care, and (3) a third person was injured because of the existing condition.[187]

In determining the applicability of the public use exception to Smith's scenario, the court explained that the dispositive issue is whether the employee qualifies as a "third person."[188] The court noted that a landlord may be "liable to a 'third person' when the property is leased for public use because the third person is there at the invitation of both the landlord and the tenant."[189] However, in ruling that summary judgment was appropriate, the court concluded that the employee did not qualify as a "third person" under the public use exception because: 1) the lease gave the tenant complete possession and control; 2) the employee was on the premises at the time of her injury; and 3) the employee was

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185. *Id.* at 217 (quoting Rogers v. Grunden, 589 N.E.2d 248, 254 (Ind. Ct. App. 1992) (citations omitted)).

186. *Id.*

187. *Id.* at 217-18. The court explained that the definition of a "third person" on business premises is found in the second Restatement of Torts which states:

> "'Third persons' include all persons other than the possessor of the land, or his servants acting within the scope of their employment. It includes such servants when they are acting outside of the scope of their employment, as well as other invitees or licensees upon the premises, and also trespassers on the land, and even persons outside of the land whose acts endanger the safety of the visitor."

Id. at 218 (quoting RESTATEMENT (SECOND) OF TORTS § 344 cmt. b (1965)).

188. *Id.*

189. *Id.* (citing Walker v. Ellis, 129 N.E.2d 65, 73 (Ind. App. 1955)).

clearly acting within the scope of her employment at the time of the injury.[190]

V. Life Estates

In *Nelson v. Parker*,[191] the Indiana Supreme Court overruled earlier authority regarding the creation of a life estate. Earlier case law[192] upheld the common law rule that "a grantor could reserve an interest only for the grantor, but not for a third person, or 'stranger' to the deed. Words of reservation were not considered to be words of 'grant' and so could not create an interest in another."[193] In an opinion written by Justice Boehm, the court in *Nelson* found that a warranty deed that was "subject to a life estate" in the grantor's habitat created a valid life estate, contrary to earlier precedent.[194]

The sole issue for the supreme court was whether a deed "subject to a life estate" in a third party created a valid life estate.[195] In the case, Russell Nelson died three months after executing a warranty deed containing the following language:

> Convey and Warrant to
> RUSSELL H. NELSON, DURING HIS LIFETIME AND UPON HIS DEATH, SHALL PASS TO DANIEL NELSON.
>
> SUBJECT TO: EASEMENTS, LIENS, ENCUMBRANCES, *LIFE ESTATE IN IRENE PARKER*, AND RESTRICTIONS OF RECORD.[196]

Irene Parker, the individual subject to the life estate, had lived with Mr. Nelson for thirteen years prior to his death. Ms. Parker remained on the property after Mr. Nelson's demise. In 1994, Daniel Nelson, Russell Nelson's son, initiated an action to eject her based on the fact that no life estate had been effectively granted.[197] The lower court ruled in favor of Ms. Parker, finding that Russell Nelson "had intended to create a life estate in Parker."[198]

The court of appeals affirmed the judgment for Ms. Parker based on the grantor's intent. The court analyzed and rejected the common law rule upheld in *Ogle v. Barker*.[199] In rejecting earlier precedent, the court of appeals noted

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190. *Id.*
191. 687 N.E.2d 187 (Ind. 1997).
192. Ogle v. Barker, 68 N.E.2d 550 (Ind. 1946).
193. *Nelson*, 687 N.E.2d at 188.
194. *Id.* at 187.
195. *Id.*
196. *Id.* (emphasis added).
197. *See id.*
198. *Id.*
199. 68 N.E.2d 550 (Ind. 1946); *see Nelson*, 687 N.E.2d at 188.

that "the common law rule was derived from efforts, dating back to feudal times, to limit conveyance by deed as a substitute for livery by seisen."[200]

In affirming the lower court's decision, the Indiana Supreme Court stated that "the common law rule upheld in *Ogle* serves no practical purpose today."[201] The decision to override earlier precedent, the court noted, is in line with scholarly opinion and several other jurisdictions.[202] The court was "not persuaded that the public policy promoting settled rules requires adherence to a vestige of ancient conveyancing law that has only pernicious efforts. To the extent *Ogle* holds otherwise, it is overruled."[203]

VI. JOINT TENANCY AND TENANCY IN COMMON

Under established Indiana law, the Indiana Joint Tenancy Statute[204] governs the ownership rights incident to property held by two or more persons. A joint tenancy represents a "single estate in property owned by two or more persons under one instrument or act."[205] The requirements that must exist for a joint tenancy to be found include: "1) The tenants must have one and the same interest; 2) the interests must accrue by one and the same conveyance; 3) the interests must commence at one and the same time; and 4) the property must be held by one and the same undivided possession."[206] This statute "preserves the nineteenth century preference for tenancy in common."[207]

Under settled Indiana law regarding tenancy in common, an owner in common of personal property is permitted to sell his undivided interest; however, he is not permitted to sell or dispose of the entire property with being granted

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200. *Nelson*, 687 N.E.2d at 188.

201. *Id.* at 189.

202. *Id.* (citing Aszmus v. Nelson, 743 P.2d 377 (Alaska 1987); Borough of Wildwood Crest v. Smith, 509 A.2d 252 (N.J. Super. Ct. App. Div. 1986); Malloy v. Boetcher, 334 N.W.2d 8 (N.D. 1983); Simpson v. Kistler Inv. Co., 713 P.2d 751 (Wyo. 1986); ROGER A. CUNNINGHAM ET AL., THE LAW OF PROPERTY § 10.11, at 719 (1984); 14 RICHARD R. POWELL, POWELL ON REAL PROPERTY ch. 81A, at 119-22, 122 para. 899[3][g] (1997)).

203. *Id.* at 190.

204. IND. CODE § 32-4-1.5-15 (1998). The statute provides:

> Personal property, other than an account, which is owned by two (2) or more persons is owned by them as tenants in common unless expressed otherwise in a written instrument. However, household goods acquired during coverture and in possession of both husband and wife, and any promissory note, bond, certificate of title to a motor vehicle, or any other written or printed instrument evidencing an interest in tangible or intangible personal property, other than an account, in the name of both husband and wife, shall upon the death of either become the sole property of the surviving spouse unless a clear contrary intention is expressed in a written instrument.

Id.

205. Poulson v. Poulson, 691 N.E.2d 504, 506 (Ind. Ct. App. 1998) (citations omitted).

206. *Id.* (citing Richardson v. Richardson, 98 N.E.2d 190, 192-93 (Ind. App. 1951)).

207. *Id.*

authority to do so by his cotenants.[208] Further, when an owner in common "converts the whole to his own exclusive use or does something equivalent to an utter denial of the rights of his co-owner, he becomes liable to such co-owner for the injury thereby inflicted."[209]

In *Poulson v. Poulson*, the Indiana Court of Appeals, during the survey period, had the opportunity to address the ownership rights of jointly held property of spouses after a dissolution of marriage.[210] The Poulsons were married in April 1979. The couple separated on October 21, 1991, and the wife filed a petition for dissolution of marriage on October 25, 1991. The marriage was dissolved by court order on July 22, 1992, and the marital assets were distributed pursuant to the marital settlement agreement of the parties.[211]

In August 1996, the ex-wife filed a Rule to Show Cause alleging that the ex-husband had disposed of a 1966 dune buggy that was jointly owned by each and had failed to pay the ex-wife one-half of the value of the asset. After a hearing on the issue, the lower court found for the ex-wife and ordered that the ex-husband pay $500 to the ex-wife, which represents one-half of the value of the asset.[212]

On appeal, the sole issue involved whether the lower court abused its discretion in awarding the ex-wife one-half the value of the asset. The ex-husband argued that the lower court incorrectly modified the original dissolution decree by awarding the ex-wife one-half the value of the asset.[213] The ex-wife, however, maintained that the Indiana Joint Tenancy Statute does not apply. She argued that "since the parties held the property as tenants by the entirety during their marriage, upon dissolution they became tenants in common by operation of law."[214] Thus, she argued, she was entitled to one-half the value of the sold asset.[215]

In affirming the lower court's decision, the Indiana Court of Appeals explained that it "has long been held in this state that a final decree of dissolution converts a tenancy by the entirety into a tenancy in common with both spouses taking equal shares."[216] However, the court explained that "it has also been held that estates by entireties do not exist as to personal property except when such

208. *See id.* (citing Sims v. Dame, 15 N.E. 217, 219 (Ind. 1888)).

209. *Id.* (citing *Sims*, 15 N.E. at 219).

210. *Id.* at 504.

211. *See id.* at 505.

212. *Id.*

213. *See* IND. CODE § 31-1-11.5-17(b) (1993) (recodified at IND. CODE § 31-15-7-9.1 (1998)). The court explained that this section "governs the modification of property disposition and states that property disposition orders entered under final decrees may not be revoked or modified, except in case of fraud which must be asserted within six years after the order is entered." *Poulson*, 691 N.E.2d at 505.

214. *Poulson*, 691 N.E.2d at 505.

215. *See id.*

216. *Id.* at 506 (citing IND. CODE § 32-4-2-2 (1993) (recodified at IND. CODE § 32-4-2-2 (1998))).

property is directly derived from real estate held by that title."[217]

Applying the Indiana Joint Tenancy Statute to the instant case, the court found that the ex-wife and ex-husband had owned the dune buggy as joint tenants with the right of survivorship, not tenants by the entirety.[218] The court reasoned that the individuals' joint tenancy status is dependant upon the continuation of the marriage relation and that by statute, the law presumes that such property is held by spouses as joint tenants.[219] In this case, however, the court explained that the evidence revealed that the asset, acquired during marriage and titled to both spouses, was not disposed of in the original dissolution decree.[220] Upon the dissolution of marriage and the failure of the property to be disposed of in the divorce decree, the court explained that "the joint tenancy was severed and [the spouses] became owners of the dune buggy as tenants in common with each spouse sharing equally in the property."[221] Thus, the court affirmed the lower court's decision by concluding that because "Husband disposed of the dune buggy without Wife's permission and failed to deliver any part of the value to Wife, Wife was entitled to one-half the value of the dune buggy."[222]

VII. Water Rights

A. Common Enemy Doctrine

In *Trowbridge v. Torabi*,[223] the Indiana Court of Appeals had the opportunity to affirm that Indiana continues to adhere to the "common enemy doctrine." The Indiana Supreme Court has encapsulated the doctrine as follows:

> In its most simplistic and pure form the rule known as the "common enemy doctrine," declares that surface water which does not flow in defined channels is a common enemy and that each landowner may deal with it in such manner as best suits his own convenience. Such sanctioned dealings include walling it out, walling it in and diverting or accelerating its flow by any means whatever.[224]

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217. *Id.* (citing Koehring v. Bowman, 142 N.E. 117, 118 (Ind. 1924)).
218. *Id.*
219. *Id.*
220. *Id.* at 507.
221. *Id.*
222. *Id.*
223. 693 N.E.2d 622 (Ind. Ct. App. 1998).
224. *Id.* at 627 (quoting Argyelan v. Haviland, 435 N.E.2d 973, 975 (Ind. 1982)). An exception to the common enemy doctrine (or more accurately, a limiting principle to the doctrine) was stated by the court in *Pickett v. Brown*: "[O]ne may not collect or concentrate surface water and cast it, in a body, upon his neighbor." 569 N.E.2d 706, 708 (Ind. Ct. App. 1991) (quoting *Argyelan*, 435 N.E.2d at 976). *See also* Gene B. Glick Co. v. Marion Constr. Corp., 331 N.E.2d 26, 31 (Ind. App. 1975) (stating that one "cannot, by means of drains and ditches, concentrate surface water, and by that means carry it where it never flowed before, and discharge it onto a lower land-owner to his damage").

Therefore, under the common enemy doctrine, it is permissible "for a landowner to improve his land in such a manner as to accelerate or increase the flow of surface water by limiting or eliminating ground absorption or changing the grade of the land."[225]

Trowbridge involved a dispute among three owners of adjacent properties. A pond is located on all three properties, but is principally located on property owned by the Torabis. In 1995, the Torabis constructed a stone driveway across the pond for the purpose of gaining access to a landlocked part of their property. The Trowbridges and the Hamiltons (collectively "the Trowbridges") filed a complaint, alleging that the construction of the driveway caused damage to their property.[226] The Trowbridges based their claims for damages on theories of nuisance and trespass.[227] The trial court granted summary judgment in favor of the Torabis, finding that "the laws of property rights and water rights apply and not the law of nuisance."[228]

The court of appeals initially recognized the need to "classify" the water at issue in the case, stating that "[d]ifferent 'water rights' attach depending on whether water is classified as a private pond, a common private pond, a natural watercourse, or mere surface water."[229] If the body of water at issue is classified as surface water, then nuisance law would not apply.[230] However, if the body of water is labeled a private pond, a common private pond, or a natural water course, then nuisance law might apply.[231] The classification of the water at issue in *Trowbridge* was particularly relevant because if it was classified as surface water, the common enemy doctrine could apply to shield the Torabis from liability for damage caused by the construction of the driveway.

The court held that the trial court's grant of summary judgment in favor of the Torabis was erroneous in that genuine issues of material fact existed with regard to whether the Torabis were liable for damage to the adjacent properties.[232] Specifically, the court stated that "if the water involved is mere surface water, then, pursuant to the common enemy doctrine, the Torabis are not liable for the alleged damage . . . and the Trowbridges and Hamiltons may not circumvent the well-settled laws pertaining to surface waters by characterizing

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225. *Pickett*, 569 N.E.2d at 707; *Trowbridge*, 693 N.E.2d at 626 (citing *Argyelan*, 435 N.E.2d at 973. *See also* Cloverleaf Farms, Inc. v. Surratt, 349 N.E.2d 731, 732 (Ind. App. 1976) (stating that a landowner may improve his property so as to cause surface water to stand in unusual quantities on other adjacent land).

226. *See Trowbridge*, 693 N.E.2d at 623-24.

227. *See id.* at 624.

228. *Id.* at 625.

229. *Id.* at 626.

230. *See id.*

231. *See id.* The court in *Trowbridge* proceeded to define the terms "surface water," "pond," "private pond," and "natural watercourse," and also discussed the rights and liabilities of adjacent landowners with respect to each classification. *Id.* at 626-28.

232. *Id.* at 628.

their cause of action as one based upon a nuisance."[233] On the other hand, the court continued, "if the water is a common private pond and not mere surface water, then . . . the Torabis may be liable for damages based upon a nuisance theory . . . ."[234] The court determined that factual issues existed that could not be resolved on the present record, and therefore remanded the case to the trial court.[235]

B. Ground Water Removal

In *City of Valparaiso v. Defler*,[236] the court of appeals addressed an issue of first impression in Indiana. *Defler* addressed the issue of "whether a landowner's right to remove ground water from his property shields him from liability for subsidence damage to adjoining land caused by the water's removal."[237] In *Defler*, landowners filed a lawsuit against the City of Valparaiso (the "City"), its Board of Public Works, McMahon Associates, Inc., and Woodruff & Sons, Inc. The landowners alleged that in the course of designing and constructing a sewer lift station adjacent to their property, the defendants caused their land to subside.[238] The City filed a motion for summary judgment, which the lower court denied. This interlocutory appeal followed.[239]

In affirming the lower court's decision, the Indiana Court of Appeals explained that "[t]wo general theories have developed in the United States regarding the ownership and use of ground water."[240] These theories include: 1) the English Rule, or the absolute dominion rule; and 2) the American Rule, or the reasonable use rule.[241] The English Rule, "provides that ground water is part of the land and the landowner has the absolute right to use the water as he wishes. This absolute right allows the owner of land to remove ground water regardless of the damage caused to neighboring property owners."[242]

The American Rule, on the other hand, "provides that where the rights of others are affected by a landowner's use of ground water, his use is limited to a 'reasonable and beneficial use' or to 'some useful purpose connected with its occupation and enjoyment.'"[243] Thus, under the American Rule, the actual effect that the use of ground water has on neighboring landowners is considered.[244]

Indiana is among only ten states that continue to follow some version of the

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233. *Id.*
234. *Id.*
235. *Id.* at 629.
236. 694 N.E.2d 1177 (Ind. Ct. App. 1998).
237. *Id.* at 1179.
238. *See id.* at 1178-79.
239. *Id.* at 1178.
240. *Id.* at 1179 (citation omitted).
241. *See id.*
242. *Id.* (citation omitted).
243. *Id.* at 1180.
244. *See id.*

English Rule.[245] After analyzing Indiana case law regarding the issue,[246] the court "decline[d] to interpret Indiana's version of the English Rule in a manner which would essentially place the right to remove ground water from one's property above the right of an adjoining landowner to the subjacent support of his land."[247] The court explained that its refusal to strictly follow the English Rule is "bolstered by the clear trend in this state and in other jurisdictions toward ameliorating the often harsh consequences which can result from strict application of the English Rule."[248] The court held that "Indiana's law regarding the ownership and use of ground water does not shield the City from liability for subsidence damage caused by the City's removal of the water."[249]

VIII. Zoning

During the survey period, a number of zoning cases reached the appellate courts. Several cases involved appeals from decisions of various zoning boards—some discussed the standard for reviewing those decisions,[251] while others assessed a party's standing to challenge a board's decision.[252] In

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245. *See id.* (citations omitted).

246. *See* Wiggins v. Brazil Coal & Clay Corp., 452 N.E.2d 958, 964 (Ind. 1983) (holding that the right to the use of ground water does not extend to causing injury gratuitously or maliciously to the nearby lands).

247. *Defler*, 694 N.E.2d at 1182.

248. *Id.*

249. *Id.* The court also addressed the applicability of the Indiana Tort Claims Act ("ITCA") to the case. The court found that "the trial court properly denied the City's motion for summary judgment based upon its claim of immunity under the ITCA." *Id.* at 1183.

251. *See* Scott v. Marshall County Bd. of Zoning Appeals, 696 N.E.2d 884, 885 (Ind. Ct. App. 1998) (stating that "[o]nly if the Board's decision is arbitrary, capricious or an abuse of discretion should it be reversed" and recognizing that this places a "heavy burden" on a party petitioning to overturn the Board's decision); Rush County Bd. of Zoning Appeals v. Ryse, 686 N.E.2d 186, 186-87 (Ind. Ct. App. 1997) (stating that "[w]hen reviewing a decision of the Board of Zoning Appeals the trial court must determine if the board's decision was incorrect as a matter of law" and "'[u]nless the Board's decision was illegal, it must be upheld'" (quoting Board of Zoning Appeals v. Kempf, 656 N.E.2d 1201, 1203 (Ind. Ct. App. 1995))). The court in *Scott* held that the board reasonably denied a property owner's request for special exception to construct and operate a dog kennel on land zoned for agriculture. *Scott*, 696 N.E.2d at 887. The property owners were already housing several dogs and neighbors had complained that noise from the dogs was already a problem. *See id.*

252. *See* Robertson v. Board of Zoning Appeals, 699 N.E.2d 310, 315-16 (Ind. Ct. App. 1998) (holding that a grocery store owner did not waive the right to challenge standing of the landowner and neighborhood association to challenge a board decision to grant a variance by failing to object to standing during the initial hearing before the board). In *Robertson*, the court ultimately found that both the landowner and the neighborhood association lacked standing to challenge the board's granting of the variance. *Id.* at 316-17. *See also* City of New Haven v. Allen County Bd. of Zoning, 694 N.E.2d 306, 312-13 (Ind. Ct. App. 1998) (finding that a city adjoining a landfill was

Brownsburg Conservation Club, Inc. v. Hendricks County Board of Zoning Appeals,[253] the court reviewed the board's revocation of a variance that had been previously issued. The court explained that "[a] variance affords relief from the enforcement of a zoning ordinance and permits use of property which the ordinance otherwise forbids."[254] The court then pointed out that while "the initial grant or denial of a variance rests within the discretion of the board of zoning appeals, a zoning board has no inherent authority to revoke a variance once issued."[255] However, the court continued, "because a zoning board is expressly authorized to impose reasonable conditions when it first approves a variance, the board has implied authority to revoke a variance if the conditions have not been satisfied."[256] The court held that the board "erred in failing to give the [property owners] notice and an opportunity to be heard on the question of whether the conditions for approval ha[d] been met" and also that the board "erred in failing to enter findings of fact to support its decision."[257] This case demonstrates the care with which a zoning board must proceed when making the decision to revoke a variance, given that a landowner may have invested substantial sums in reliance on the variance.[258]

Other decisions handed down during the survey period discussed particular uses of property. Some discussed whether particular uses were permissible given local ordinances or zoning classifications,[259] while others addressed the triggering of use permit requirements given the particular language of the applicable zoning ordinances.[260] The court of appeals also addressed the constitutionality of fines

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not an "aggrieved" party under the Planning and Development Act, and therefore lacked standing to challenge the board's settlement of several lawsuits concerning the landfill's operations).

253. 697 N.E.2d 975 (Ind. Ct. App. 1998)

254. *Id.* at 977 (citing Hazel v. Metropolitan Dev. Comm'n, 289 N.E.2d 308 (Ind. App. 1972)).

255. *Id.* (citing Ash v. Rush County Bd. of Zoning Appeals, 464 N.E.2d 347, 350 (Ind. Ct. App. 1984)).

256. *Id.* (citing Schiehuser v. City of Seymour, 674 N.E.2d 1009, 1014 (Ind. Ct. App. 1996)).

257. *Id.* at 978.

258. *See* Danaya C. Wright, *Trains, Trails, and Property Law: Indiana Law and the Rails-to-Trails Controversy*, 31 IND. L. REV. 753, 778-79 (1998) (discussing *Schlehuser*, 674 N.E.2d at 1009, and the procedural safeguards to landowners provided therein).

259. *See* Discovery House, Inc. v. Metropolitan Bd. of Zoning Appeals, 701 N.E.2d 577 (Ind. Ct. App. 1998) (construing language of zoning ordinance and finding methadone treatment facility's operations to be a "permitted use" under the ordinance); Board of Zoning Appeals v. Leisz, 686 N.E.2d 935, 937-40 (Ind. Ct. App. 1998) (finding landlord's "nonconforming use" of rental property to be permissible in that the use was legal when commenced and it was continuous from the effective date of the applicable restrictive zoning ordinance).

260. *See* Brennan v. Board of Zoning Appeals, 695 N.E.2d 983 (Ind. Ct. App. 1998) (construing definitions contained in zoning code and finding that use permit requirement was triggered); Ad Craft, Inc. v. Board of Zoning Appeals, 693 N.E.2d 110 (Ind. Ct. App. 1998) (interpreting language of ordinance requiring use permit for erection of sign, finding that "sign" includes both the message and the frame or structure displaying the message, and holding that

imposed on property owners for failure to comply with zoning ordinances.[261]

In *Wallace v. Brown County Area Plan Commission*,[262] the court was faced primarily with a constitutional issue; however, the case involved an interesting zoning ordinance. In *Wallace*, the Brown County Area Plan Commission and Board of Zoning Appeals filed a complaint for injunctive relief against the Wallaces seeking the removal of a neon sign from the window of the Wallaces' restaurant in Nashville, Indiana.[263] The Wallaces claimed that the ordinance prohibiting neon signs amounted to an unconstitutional restriction of commercial speech.[264]

The court proceeded with a discussion of commercial speech doctrine under the framework of the U.S. Supreme Court's decision in *Central Hudson Gas & Electric Corp. v. Public Service Commission*.[265] In finding the zoning ordinance banning the use of neon signs constitutional, the court concluded that the ordinance directly advanced the town's interests of safety and aesthetics, as evidenced by the unique scenic and architectural characteristics of the town.[266] Further, the court held that the ban of neon signs was "no more extensive than necessary to further the [t]own's interests in safety and aesthetics."[267] The court agreed with the trial court's statement that "'[o]ther reasonable alternatives are open to the Wallaces, such as ground lighted signs which would not contrast with the aesthetic aspects of the community the ordinance seeks to preserve.'"[268] Therefore, the ordinance was upheld.

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alteration of a sign triggers the requirement of obtaining a use permit).

261. *See* Ritz v. Area Planning Comm'n, 698 N.E.2d 386 (Ind. Ct. App. 1998) (finding a fine excessive in that it exceeded statutory authority and misinterpreted language of statute authorizing the fine).

262. 689 N.E.2d 491 (Ind. Ct. App. 1998).

263. *Id.* at 492.

264. *See id.*

265. *Id.* at 493-94 (discussing Central Hudson Gas & Elec. Corp. v. Public Serv. Comm'n, 447 U.S. 557 (1980)). In *Central Hudson*, the Supreme Court set forth a four-part test for determining the validity of government restrictions on commercial speech:

> (1) The First Amendment protects commercial speech only if that speech concerns lawful activity and is not misleading. A restriction on otherwise protected commercial speech is valid only if it (2) seeks to implement a substantial government interest, (3) directly advances that interest, and (4) reaches no further than necessary to accomplish the given objective.

Id. at 493 (citing *Central Hudson Gas & Elec.*, 447 U.S. at 566; Metromedia, Inc. v. City of San Diego, 453 U.S. 490, 507 (1981)).

266. *Id.* at 493-94.

267. *Id.* at 494.

268. *Id.*

1998 DEVELOPMENTS IN INDIANA TAXATION

LAWRENCE A. JEGEN, III*
GREGORY J. DUNCAN**

INTRODUCTION

Both the 110th Indiana General Assembly and the Indiana Tax Court contributed changes and clarifications to all of the major, and many of the minor, Indiana tax laws in 1998. This Article highlights the more interesting developments for the period of October 1, 1997 through September 30, 1998.

I. GENERAL ASSEMBLY LEGISLATION

There were hundreds of 1998 legislative changes that impacted Indiana taxation, many of which had a direct effect on both broad and narrow segments of Indiana residents. Many of the changes were attempts to fine-tune existing laws, but significant policy changes surfaced in the following major areas: state offices and administration; state and local income taxes; sales and use taxes; and property taxes.

A. Tax Administration

The general assembly enacted one bill containing four provisions that have an impact on tax administration.[1] The first provision establishes a registration center[2] that is charged with servicing the registration of commercial motor vehicles by the owners.[3] The motor carrier services division of the Indiana Department of State Revenue ("IDSR") is to supervise the registration center.[4] The new law also establishes the motor carrier regulation fund to pay for the development and operation of the registration center.[5] The funds are not to be used for gasoline tax or special fuel tax administration, as had been done prior to the new law. In addition, the new law provides for an extension of time to file a claim for a refund if a taxpayer's federal income tax liability is modified by the Internal Revenue Service ("IRS") and if the modification results in a reduction of the tax legally due.[6] Normally, a claim for a refund must be filed within three years after the later of the due date of the return or the date of payment.[7] The

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* Thomas F. Sheehan Professor of Tax Law and Policy, Indiana University School of Law—Indianapolis. B.A., Beloit College; M.B.A., J.D., University of Michigan; LL.M., New York University.

** J.D. Candidate, 1999, Indiana University School of Law—Indianapolis; B.S., 1996, Purdue University.

1. H.R. 1157, 110th Leg., 2d Reg. Sess. §§ 16, 17, 19, 26 (Ind. 1998).
2. *See* IND. CODE § 6-8.1-4-4(a) (1998) (eff. Mar. 13, 1998).
3. *See id.*
4. *See id.* § 6-8.1-4-4(b).
5. *Id.* § 8-2.1-23-1.
6. *Id.* § 6-8.1-9-1(f) (eff. Jan. 1, 1999).
7. *See id.* § 6-8.1-9-1(a).

new law extends the amount of time to file a claim for a refund to the later of the normal three-year period or six months after the taxpayer is notified of the modification by the IRS.[8] The final change made with respect to tax administration allows Indiana taxpayers to elect to round amounts reported on a return to the nearest whole dollar.[9] If the amount is greater than or equal to fifty cents, then the amount may be rounded up to the nearest whole dollar;[10] and, if the amount is less than fifty cents, then the amount may be rounded down to the nearest whole dollar.[11] By the literal terms of the statute, a taxpayer is allowed to pick and choose which items or amounts the taxpayer wants to round, which could nominally decrease the amount of a taxpayer's liability. However, this provision is in conformity with federal filing provisions and is expected to have a minimal impact on collections.

B. Gross Income Taxation

In the area of income taxation, the general assembly enacted one bill that contained four key provisions.[12] The first provision is a conforming amendment that changes a reference to the taxation of a small business' gross income to the federal law, which defines "passive investment income."[13] The second provision changes the dates for quarterly payment of gross income tax by withholding agents.[14] Had the law not been changed, a withholding agent would have been required to make only yearly payments. The general assembly also changed all references in the Indiana Code to the Internal Revenue Code ("IRC") as the IRC was in effect on January 1, 1998.[15] The final change in the area of income taxation requires Indiana residents to notify the IDSR of any modifications to the taxpayer's federal return or federal tax liability.[16] As the Indiana law was originally written, only nonresidents were required to notify the IDSR of such modifications.

C. Adjusted Gross Income Taxation

In the area of adjusted gross income tax, the general assembly enacted one bill that contained two key provisions.[17] The first provision specifies that the capital gain portion, rather than the ordinary income portion (as under the old law), of certain lump sum distributions are added back to adjusted gross income

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8. *Id.* §§ 6-8.1-9-1(f)(1), (2) (eff. Jan. 1, 1999).
9. *See id.* § 6-8.1-6-4.5 (retroactive to Jan. 1, 1998).
10. *See id.* § 6-8.1-6-4.5(1).
11. *See id.* § 6-8.1-6-4.5(2).
12. H.R. 1157, 110th Leg., 2d Reg. Sess. §§ 1, 2, 4, 5 (Ind. 1998).
13. IND. CODE § 6-2.1-3-24.5(c) (1998) (retroactive to Jan. 1, 1998).
14. *Id.* § 6-2.1-6-3.1 (retroactive to Jan. 1, 1998).
15. *See id.* § 6-3-1-11 (retroactive to Jan. 1, 1998).
16. *See id.* § 6-3-4-6 (retroactive to Jan. 1, 1998).
17. H.R. 1157, 110th Leg., 2d Reg. Sess. §§ 3, 13 (Ind. 1998).

for state tax purposes.[18] For purposes of the financial institutions tax, the second provision adds a deduction from income concerning bad debt reserves for building and loan associations, mutual savings banks, and certain cooperative banks to correspond to federal tax law.[19] Federal tax law changed the way in which thrifts calculate their allowable bad debt deductions for federal tax purposes, and Indiana merely conformed its laws to correspond to the federal change. The new deduction will accommodate accounting method changes required under the IRC for federal and state saving institutions. Without the change, Indiana would realize a windfall for taxing the recapture income from the savings institutions.

D. Sales and Use Taxation

In the area of sales and use taxation, the general assembly enacted into law one bill that contained three key provisions.[20] The first provision provides that hard cider is an alcoholic beverage if the cider has at least .5%, but not more than 7%, of alcohol by volume.[21] "Hard cider" is defined as a wine, "except for alcoholic beverage tax purposes."[22] The new law creates a hard cider excise tax at a rate of $0.115 per gallon upon the manufacture, sale, or gift of hard cider within Indiana.[23] As a result of the new law, the excise tax with respect to hard cider is now the same as the excise tax with respect to beer. The wine excise tax rate is $0.47 per gallon. Thus, the new law reduces the excise tax rate on hard cider by $0.355 per gallon.

E. Tax Credits

In the area of tax credits, the general assembly enacted one bill that allows for two tax credits.[24] The first credit is titled "Military Base Recovery Tax Credit." The new law establishes a state tax credit for rehabilitation of buildings that are located on military base facilities designated by the Indiana Enterprise Zone Board if a qualified investment is made.[25] The credit is nonrefundable but may be carried forward to future years and applied against future state tax liability.[26] The credit is based on the amount of qualified investment for the rehabilitation of a building. For buildings between twenty and thirty years old, the credit is equal to 15% of the qualified investment;[27] for buildings between

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18. IND. CODE § 6-3-1-3.5(a)(7) (1998) (retroactive to Jan. 1, 1998).
19. *Id.* § 6-5.5-1-2(a)(2)(D) (retroactive to Jan. 1, 1998).
20. H.R. 1157, 110th Leg., 2d Reg. Sess. §§ 21, 22, 24 (Ind. 1998).
21. IND. CODE § 7.1-1-3-9.5(2) (1998) (eff. July 1, 1998).
22. *Id.* § 7.1-1-3-49 (eff. July 1, 1998).
23. *Id.* § 7.1-4-4.5-1 (eff. July 1, 1998).
24. H.R. 1319, 110th Leg., 2d Reg. Sess. §§ 2, 3, 14, 16, 20 (Ind. 1998).
25. IND. CODE § 6-3.1-11.5-18(a) (1998) (retroactive to Jan. 1, 1998).
26. *See id.* §§ 6-3.1-11.5-19(a), (b).
27. *See id.* § 6-3.1-11.5-1(1).

thirty and forty years old, the credit is equal to 20% of the qualified investment;[28] and for buildings at least forty years old, the credit is equal to 25% of the qualified investment.[29] Any part of the credit may be assigned to a lessee of the recovery site.[30] Additionally, a taxpayer who substantially reduces or ceases operations in another area of Indiana in order to relocate within the military base recovery site may not claim the credit.[31] This limitation prevents a taxpayer from claiming the credit if the taxpayer was motivated to relocate only to take advantage of the credit. In essence, the credit was established to enhance economic development and not to provide a credit to taxpayers who merely relocate their business operations, which does little to benefit the economy.

The second tax credit is titled the "Community Revitalization Enhancement District Tax Credit." The new law grants a taxpayer a credit against both Indiana and local tax liability if a qualified investment is made.[32] The amount of the credit equals 25% of the qualified investment.[33] The tax credit is available for a qualified investment made for the redevelopment or rehabilitation of property that is located within a community revitalization enhancement district in a county having a population of individuals between 108,950 and 112,000, e.g., Monroe County or a municipality in Monroe County.[34] To be designated a "district," Monroe County is required to submit an application to the Advisory Commission on Industrial Development.[35] For the advisory commission to designate an area as a district, the commission must find all of the following: the area contains a building or buildings with at least one million square feet that is vacant or about to become vacant due to relocation of an employer;[36] at least 1000 fewer persons are employed currently as compared to the prior ten-year period;[37] there are significant obstacles to redeveloping the area, including obsolete buildings and infrastructure, utility problems, accessibility problems, topographical obstacles or environmental contamination;[38] the unit has expended, appropriated, pooled, set aside, or pledged at least $100,000 for purposes of addressing the redevelopment obstacles;[39] and the area is located in a county having a population of individuals between 108,950 and 112,000.[40] Additionally, an area can only be designated a "district" for a period of up to fifteen years.[41] The law

28. *See id.* § 6-3.1-11.5-1(2).
29. *See id.* § 6-3.1-11.5-1(3).
30. *See id.* § 6-3.1-11.5-18(c).
31. *See id.* § 6-3.1-11.5-23.
32. *Id.* § 6-3.1-19-3(a) (eff. Jan. 1, 1999).
33. *See id.* §6-3.1-19-3(b).
34. *See id.* § 36-7-13-12(b)(5) (eff. July 1, 1998).
35. *See id.* § 36-7-13-10(a).
36. *See id.* §§ 36-7-13-12(b)(1)(A), (B).
37. *See id.* § 36-7-13-12(b)(2).
38. *See id.* §§ 36-7-13-12(b)(3)(A) to (F).
39. *See id.* § 36-7-13-12(b)(4).
40. *See id.* § 36-7-13-12(b)(5).
41. *See id.* § 36-7-13-12(c).

also provides that a "unit," the person or persons redeveloping the area, may issue bonds to finance the cost of addressing redevelopment obstacles or problems.[42] Thus, it need not be the unit's own money that the unit is pledging to cure the defects with the redevelopment area. Like the military base recovery tax credit, the revitalization credit is a nonrefundable credit that can be carried forward against any future state tax liability,[43] and any part of the credit may be assigned to a lessee of the redeveloped property.[44] In addition, a taxpayer who substantially reduces or ceases operations in another area of the state in order to relocate within the district may not claim the credit.[45] Notwithstanding the limitation on the availability of the credit, a taxpayer may claim the credit if the taxpayer had existing operations within the district and the relocation represents an expansion of the taxpayer's operations within the district.[46]

F. Local Option Taxes

With respect to local option taxes, the general assembly enacted a law that contains three key provisions.[47] The first of these provisions permits a county having a population of individuals between 37,000 and 37,800,[48] e.g., Jackson County, to impose a County Adjusted Gross Income Tax ("CAGIT") at a rate of 1.1% on adjusted gross income for not more than four years.[49] After the county imposes the CAGIT for four years, the rate must be reduced to 1.0%.[50] The funds generated by the additional 0.1% must be used to pay the costs of operating and maintaining a jail and juvenile detention center opened in 1998.[51]

The new law also allows a county having a population between 12,600 and 13,000,[52] e.g., Pulaski County, to impose a CAGIT at a rate of 1.3%.[53] The gross revenues from the additional 0.3% must be used to pay the costs of operating and maintaining a jail and justice center.[54] However, with respect to this credit, there is no requirement that the jail and justice center be opened after a specific date in order to use the funds. The new law permits a CAGIT rate of 1.3% for four years, and after the four-year period, requires the county to reduce its CAGIT rate to 1.0%.[55] The new law also provides that the county council may decrease the

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42. *Id.* § 36-7-13-16(a).
43. *See id.* § 6-3.1-19-4.
44. *See id.* § 6-3.1-19-3(c).
45. *See id.* § 6-3.1-19-5.
46. *See id.* §§ 6-3.1-19-5(1), (2).
47. H.R. 1157, 110th Leg., 2d Reg. Sess. §§ 7, 8, 11 (Ind. 1998).
48. IND. CODE § 6-3.5-1.1-2.5(a) (1998) (eff. July 1, 1998).
49. *Id.* § 6-3.5-1.1-2.5(c).
50. *See id.*
51. *See id.* § 6-3.5-1.1-2.5(d)(2).
52. *Id.* § 6-3.5-1.1-3.5(a) (eff. Mar. 13, 1998).
53. *Id.* § 6-3.5-1.1-3.5(c).
54. *See id.* § 6-3.5-1.1-3.5(d)(2).
55. *Id.* § 6-3.5-1.1-3.5(c).

tax rate or rescind the tax in the same manner as other reductions or rescissions under the county's CAGIT law.[56]

The final provision in the new law relating to local option taxes increases limits on the CAGIT plus County Economic Development Income Tax ("CEDIT") rates. Normally, a county's CAGIT plus CEDIT rate may not exceed 1.25%.[57] However, the new law increases the limit to 1.35% for the 37,000 to 37,800 population counties[58] and to 1.55% for the 12,600 to 13,000 population counties.[59]

G. *Property Taxation*

In the area of property tax, the general assembly enacted three bills.[60] The first bill[61] provides that a county having a population of between 400,000 and 700,000, e.g., Lake County, may remove real property from the list of property eligible for tax sale if the taxpayer and the county treasurer agree to a mutually satisfactory arrangement for the payment of the delinquent property taxes in full.[62] The property may be removed from the list if the agreement between the county treasurer and the taxpayer is in writing, signed by the taxpayer, and provides for full payment of delinquent taxes within one year.[63] Prior to this legislation, property could not be removed from the tax sale list until all past due tax and other costs were paid in full. However, under the new law, if the taxpayer misses a payment, the county auditor is required to place the property back on the list of property eligible for sale at a tax sale.[64]

The new law also allows cities having a population between 110,000 and 120,000,[65] 33,850 and 35,000,[66] and 75,000 and 90,000,[67] e.g., Gary, Hammond, and East Chicago, to offer property within their jurisdiction for sale at an expedited second tax sale if the property fails to receive the minimum amount in a county tax sale and the county auditor and city mayor agree to such an expedited tax sale.[68] Additionally, the new law allows cities such as Gary, Hammond, and East Chicago to acquire a lien and a tax sale certificate if the

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56. *Id.* §§ 6-3.5-1.1-2.5(c) (eff. July 1, 1998), 6-3.5-1.1-3.5(c) (eff. Mar. 13, 1998).
57. *See id.* § 6-3.5-7-5(c).
58. *Id.* § 6-3.5-7-5(h).
59. *Id.* § 6-3.5-7-5(i).
60. H.R. 1002, 110th Leg., 2d Reg. Sess. §§ 1-6 (Ind. 1998); H.R. 1272, 110th Leg., 2d Reg. Sess. §§ 1, 3, 4, 6, 7, 10, 12, 13 (Ind. 1998); S. 327, 110th Leg., 2d Reg. Sess. §§ 1, 2 (Ind. 1998).
61. H.R. 1272, 110th Leg., 2d Reg. Sess. (Ind. 1998).
62. IND. CODE § 6-1.1-24-1.2(c) (1998) (eff. July 1, 1998).
63. *See id.* § 6-1.1-24-1.2(d).
64. *Id.* § 6-1.1-24-1.2(e).
65. *Id.* § 6-1.1-24-5.6(a)(1) (eff. July 1, 1998) (expires June 30, 2001).
66. *Id.* § 6-1.1-24-5.6(a)(2).
67. *Id.* § 6-1.1-24-5.6(a)(3).
68. *Id.* § 6-1.1-24-5.6(c).

property is not sold at the city's tax sale.[69] Under the new law, if the property is sold to a purchaser or acquired by the city, then the deed would be transferred in 120 days, if the property is not redeemed by then.[70] However, the county auditor is not required to issue a deed to the city if it is determined that the property contains hazardous waste.[71] Prior to the new law, the usual redemption period was one year. The shortened redemption period is intended to encourage taxpayers to pay more expeditiously. The new law grants the county the power to enter the property in order to conduct environmental investigations.[72] The proceeds from the sale of any property by the city are: First, to be applied against the costs of the sale;[73] second, to the payment of such taxes removed;[74] and third, any surplus is to be deposited in the city's general fund.[75] The fiscal body, e.g., of Gary, Hammond, and East Chicago, must approve sales of property valued at $10,000 or greater, leases with annual payments of at least $5000, transfers of gift property back to the grantors, and transfers to a neighborhood development corporation.[76]

In a noncode provision, the new law allows the cities, e.g., of Gary, Hammond, and East Chicago, to conduct an additional tax sale of properties within the city's jurisdiction on which at least six property tax installments are delinquent.[77] All of these provisions are expected to help the cities, e.g., Gary, Hammond, and East Chicago and Lake County, to quickly sell or otherwise dispose of real property on which there is a property tax delinquency. This provision is intended to help get taxable property back onto the tax rolls sooner and should reduce long-term collection expenses and increase the cash flow to the cities and county. The fact that the cities can take possession of the property may also encourage some taxpayers to pay in a more timely fashion.

The second bill[78] contained two key provisions. The first provision requires a county auditor to include the name of the owner of a tract of real property eligible for sale at a tax sale in the notice of the tax sale.[79] If the property is owned by more than one individual, then the name of at least one owner must be included in the notice of the tax sale.[80] Prior to this legislation, when parcels of real property went to tax sale, the county auditor had to prepare a notice that included various information such as a list of parcels for sale, the minimum sale

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69. *Id.* §§ 6-1.1-24-6.6(b), (c) (eff. July 1, 1998) (expires June 30, 2001).
70. *Id.* §§ 6-1.1-25-4.2(b), (c) (eff. July 1, 1998) (expires Sept. 30, 2001).
71. *See id.* § 6-1.1-25-4(e) (eff. July 1, 1998).
72. *See id.*
73. *See id.* § 6-1.1-25-9.5(b)(1) (eff. July 1, 1998) (expires Dec. 31, 2001).
74. *See id.* § 6-1.1-25-9.5(b)(2).
75. *See id.* § 6-1.1-25-9.5(b)(3).
76. *See id.* §§ 36-1-11-3.2(b)(1) to (3) (eff. July 1, 1998).
77. H.R. 1272, 110th Leg., 2d Reg. Sess. § 13 (Ind. 1998) (eff. Mar. 13, 1998) (expires Jan. 1, 2001).
78. S. 327, 110th Leg., 2d Reg. Sess. (Ind. 1998).
79. IND. CODE § 6-1.1-24-2(a)(6)(A) (1998) (eff. July 1, 1998).
80. *See id.* § 6-1.1-24-2(a)(6)(B).

price, and information regarding redeeming the property, but not the name of the owner of the property.[81] Most counties already include the property owner's name in the tax sale notice, but for those counties that do not, the county is now required to include such information in the notice. The second provision requires the county auditor to mail a copy of a tax sale notice by certified mail, return receipt requested, to a mortgagee who requests by certified mail a copy of the notice.[82] Prior to the new law, the county auditor was required to mail a copy of a tax sale notice to a requesting mortgagee by certified mail. Now, the county auditor must mail such notice by certified mail, return receipt requested.[83]

The third new law[84] enacted by the general assembly relating to property taxes has five important provisions. The first provision requires a county to notify a taxpayer, by mail, at the taxpayer's last known address, that the taxpayer overpaid taxes before the excess tax payment may be transferred to the county general fund.[85] Prior to this new law, if a taxpayer overpaid a local tax or special assessment, the taxpayer could file a claim for refund within three years after November tenth of the year during which the payment was made.[86] The new law requires a county treasurer to give written notice to taxpayers who made overpayments of more than $5.00.[87] The notice must include all of the following: a statement that the taxpayer may be entitled to a refund because of an overpayment;[88] the amount of the refund;[89] instructions for claiming the refund;[90] the date on or before which the refund must be claimed;[91] and, a statement that the refund will be reduced by any amount which is applied to property taxes which are delinquent.[92] The notice is intended to increase the likelihood that a taxpayer will file a claim for refund for an overpayment of taxes.

The second provision provides that, before an owner records a transfer of ownership for a property interest that is created from a larger existing parcel or a combination of smaller existing parcels, the owner is required to pay the property taxes for which the due date has passed before the county auditor may transfer the property on the last assessment list or apportion the assessed value of the property.[93] Prior to this provision, before an owner could record a transfer of ownership for such a parcel of property, the owner was required to pay all

81. *See id.* § 6-1.1-24-2(a).
82. *Id.* § 6-1.1-24-3(b) (eff. July 1, 1998).
83. *See id.*
84. H.R. 1002, 110th Leg., 2d Reg. Sess. (Ind. 1998).
85. IND. CODE § 6-1.1-26-6(d) (1998) (eff. July 1, 1998).
86. *See id.* § 6-1.1-26-6(c).
87. *Id.* § 6-1.1-26-6(d) (eff. July 1, 1998).
88. *See id.* § 6-1.1-26-6(d)(1).
89. *See id.* § 6-1.1-26-6(d)(2).
90. *See id.* § 6-1.1-26-6(d)(3).
91. *See id.* § 6-1.1-26-6(d)(4).
92. *See id.* § 6-1.1-26-6(d)(5).
93. *Id.* § 6-1.1-5-5.5(d) (eff. July 1, 1998).

property taxes "due and owing."[94] The new law relaxes this requirement and only requires an owner to pay all property taxes that are "due" before such property can be transferred.[95]

The third provision requires an assessing official to consolidate existing contiguous parcels of real property into a single parcel if the assessing official has knowledge that an improvement to the real property is located on or otherwise significantly affects the parcels.[96] The new law added the requirement that an assessing official "have knowledge" of such an improvement before the assessing official is required to consolidate the contiguous parcels.[97]

The fourth provision provides that, in addition to serving a written demand for payment of delinquent taxes by certified or registered mail or in-person service by the treasurer or his deputy, a county treasurer may also serve a written demand "by proof of [a] certificate of mailing."[98] With respect to this change, the new law increases the fee a county treasurer can charge from $5.00 to $8.00 if registered or certified mail is used in making a demand for payment of delinquent taxes.[99]

The final provision relating to property taxes provides that property tax refunds are to be paid after the June or December settlement and apportionment of property taxes, or after both the June and December settlement and apportionment of property taxes.[100] Prior to this provision, if a refund was made to a taxpayer, the county auditor deducted the refund from the December distribution of taxes.[101] This provision grants the county auditor an optional and quicker reimbursement method of distributing tax refunds.

H. Innkeeper and Other Local Taxes

In the area of innkeeper taxes and other local taxes, the general assembly enacted three bills that contained three significant provisions.[102] The first of these provides that a county fiscal body adopting an ordinance to impose or rescind the county innkeeper's tax or to change the tax rate must send a certified copy of the ordinance to the IDSR.[103] Additionally, the new law provides that the county fiscal body adopting the ordinance must specify the effective date of the ordinance that must take effect on the first day of a month at least thirty days

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94. *Id.* § 6-1.1-5-5.5(d).
95. *Id.* § 6-1.1-5-5.5(d) (eff. July 1, 1998).
96. *Id.* § 6-1.1-5-16 (eff. July 1, 1998).
97. *Id.*
98. *Id.* § 6-1.1-23-1(a)(3) (eff. July 1, 1998).
99. *Id.* § 6-1.1-23-7(a)(1)(A) (eff. July 1, 1998).
100. *Id.* § 6-1.1-26-5(b) (eff. July 1, 1998).
101. *See id.* § 6-1.1-26-5(b).
102. H.R. 1157, 110th Leg., 2d Reg. Sess. § 20 (Ind. 1998); H.R. 1002, 110th Leg., 2d Reg. Sess. § 7 (Ind. 1998); H.R. 1097, 110th Leg., 2d Reg. Sess. § 6 (Ind. 1998).
103. IND. CODE § 6-9-29-1.5(b) (1998) (eff. July 1, 1998).

after adoption.[104]

The second key provision expands the use of the Allen County food and beverage tax to include new expansions of the county's coliseum. Prior to the new law, Allen County could only use money from the coliseum expansion fund as the coliseum existed on the date that the ordinance establishing the food and beverage tax was adopted. The new law allows for acquisitions, improvement, remodeling, or expansion of the coliseum as the coliseum existed before January 1, 1998.[105] The new law also clarifies that money set aside for debt reserve prior to July 1, 1998 may not be used for acquisition, improvement, remodeling, or expansion of the coliseum.[106] The third provision requires the city-county council of a consolidated first class city, e.g., Indianapolis, to offer tickets for sale to the public by a "box office at the facility" or through "an authorized agent of the facility" before the council can impose a county admissions tax on the sale of tickets to an event.[107]

I. Tax On Financial Institutions

In the area of tax on financial institutions, the general assembly enacted one bill containing one key provision.[108] The new law changes a reference to the provisions under which trust companies are established.[109] Because of the change, a regulated financial corporation in Indiana includes a trust company that is formed under Indiana Code section 28-12.[110]

II. Indiana Tax Court Opinions and Decisions

A. Indiana Property Taxes—Real Property Taxes

1. Town of St. John v. State Board of Tax Commissioners ("*St. John III*").[111]—This case originated when the plaintiffs filed suit and the tax court held that Indiana's property tax assessment system violated the Indiana Constitution.[112] However, the Indiana Supreme Court reversed the tax court decision and remanded the case for a determination of whether Indiana's assessment "system results in a uniform and equal rate of assessment and a just

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104. *Id.* § 6-9-29-1.5(a).

105. *Id.* § 6-9-23-8(a)(1)(B) (eff. July 1, 1998).

106. *Id.* § 6-9-23-8(c).

107. *Id.* §§ 6-9-13-1(a)(2)(A), (B) (eff. Mar. 11, 1998).

108. H.R. 1157, 110th Leg., 2d Reg. Sess. § 14 (Ind. 1998).

109. IND. CODE § 6-5.5-1-17(c)(8) (1998) (retroactive to Jan. 1, 1998).

110. *See id.*

111. 690 N.E.2d 370 (Ind. Tax Ct. 1997) [hereinafter *St. John III*], *supplemented*, 691 N.E.2d 1387 (Ind. Tax Ct. 1998) [hereinafter *St. John IV*], *clarified*, 698 N.E.2d 399 (Ind. Tax Ct. 1998) [hereinafter *St. John V*], *aff'd in part, rev'd in part*, 702 N.E.2d 1034 (Ind. 1998) [hereinafter *St. John VI*].

112. *St. John III*, 690 N.E.2d at 372 (citing Town of St. John v. State Bd. of Tax Comm'rs, 665 N.E.2d 965 (Ind. Tax Ct. 1996) [hereinafter *St. John I*]).

valuation based on property wealth."[113] The tax court determined the following issues on remand: (1) whether Indiana's property tax assessment system violated article X, section 1 of the Indiana Constitution; (2) whether the system violated article I, section 12 of the Indiana Constitution; (3) whether the system violated the federal Due Process Clause of the Fourteenth Amendment to the U.S. Constitution, procedurally or substantively; and, (4) whether the system violated the federal Equal Protection Clause of the Fourteenth Amendment to the U.S. Constitution.[114] The tax court discussed each issue separately.

Indiana imposes a tax on the value of real property and the value of real property is defined by statute as the "True Tax Value."[115] "'[T]rue tax value does not mean fair market value . . . [but rather] the value determined under the rules of the state board of tax commissioners.'"[116] The Indiana State Board of Tax Commissioners ("ISBTC") is required by statute to assess property according to the laws of Indiana.[117] In an attempt to execute its statutory duties, the ISBTC has promulgated regulations for determining the true tax value of real property.[118] Under the regulations, the value of non-agricultural land is determined by a county land valuation commission.[119] The county commission determines the value of land based on sales data for the county and forwards such values to the ISBTC for approval.[120] The ISBTC then either approves or modifies such values.[121] Thus, the ISBTC has final say as to the value of the property.[122] The final value of the property is reduced to a County Land Valuation Order. Therefore, the value of property as determined by the county approximates the land's fair market value because sales data is used as the basis for the county's determination of value.[123]

A county agricultural land advisory committee determines the true tax value of agricultural land[124] by starting at a base rate of $495 per acre and adjusting that rate to reflect the soil's crop production capacity.[125] Thus, the value of agricultural land approximates the land's earning capacity.[126]

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113. *Id.* (citing Town of St. John v. State Bd. of Tax Comm'rs, 675 N.E.2d 318 (Ind. 1996) [hereinafter *St. John II*]).
114. *Id.*
115. *See id.* at 372-73 (citing IND. CODE § 6-1.1-31-6(b)(7) (1998)).
116. *Id.* at 373 (quoting IND. CODE § 6-1.1-31-6(c) (1998)).
117. *See id.* (citing IND. CODE § 6-1.1-35-1 (1998)).
118. *See id.*
119. *See id.*
120. *See id.*
121. *See id.*
122. *See id.* at 373 n.2.
123. *See id.* at 373.
124. *See id.* (citing IND. CODE § 6-1.1-4-13) (1998)).
125. *See id.* (citing IND. ADMIN. CODE tit. 50, rs. 2.2-5-6(5), 2.2-5-7 (1996)).
126. *See id.* Though it appears that agricultural land is valued entirely based on the land's earning capacity, this is not true. It depends upon what factors were taken into account in determining the base rate of $495 per acre.

By regulation, the true tax value of an improvement is the cost of reproduction minus physical or obsolescence depreciation.[127] Though "[r]eproduction cost is defined as the 'whole-dollar cost of reproducing the item[,]' [t]he 'reproduction cost' of an improvement . . . is not the *actual* cost of reproducing the item. Rather, it is the 'reproduction cost' as specified in the [ISBTC's] cost schedules."[128] The cost schedules currently in effect represent 1985 reproduction costs, reduced by 15% for all items contained in the schedule.[129] The cost schedules are classified into different types of improvements and assigned a model. The model has many amenities that are assumed to exist in the property being taxed. If an amenity does not exist, as presumed in the model, or if additional amenities are present, then the value of the improvement is adjusted upward or downward to reflect the lack of similarity to the model.[130] The schedules are the only information that can be used in arriving at the improvement's true tax value.[131] The true tax value of property can only be determined by reference to ISBTC regulations; external evidence is disregarded by the ISBTC.[132] "As a result, evidence of an improvement's actual reproduction cost or evidence of the actual value of land is irrelevant under the True Tax Value system."[133]

The court next examined the claim that Indiana's property tax assessment system violated Indiana Constitution article X, section 1. The court attempted to determine the intent of the framers in requiring the legislature "to provide for a 'uniform and equal rate of property assessment and taxation,' and to secure a 'just valuation for taxation of all property, both real and personal.'"[134] In doing this, the court looked to history: "Delegate Read stated that he knew of farms 'which were of equal value assessed at a difference of fifty perc., and farms of less value than others at a much higher rate.'"[135] After examining this comment and several others, the court reached the conclusion that the delegates "evaluated [the] fairness [of article X, section 1], not by any rules of assessment, but rather based on a real world understanding about what the particular property was worth."[136] According to the court, it was apparent that the framers intended property assessments to be made based on a property's actual worth, as determined by reference to "real world values."[137]

Using the perceived intent of the framers, the court examined whether the

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127. *See id.* (citing IND. ADMIN. CODE tit. 50, rs. 2.2-2-1(c), 2.2-7-9 (1996)).

128. *Id.* (quoting IND. ADMIN. CODE tit. 50, r. 2.2-7-7.1(f)(8) (1996)).

129. *See id.* at 373 n.5.

130. *See id.* at 374.

131. *See id.*

132. *See id.*

133. *Id.*

134. *Id.* (quoting IND. CONST. art. X, § 1(a)).

135. *Id.* at 375 (quoting 1 Report of the Debates and Proceedings of the Convention for the Revision of the Constitution of State of Indiana 946 (1850)).

136. *Id.*

137. *Id.*

current tax system resulted in uniformity and equality. The ISBTC argued that the system "is an effort to provide uniformity and equality . . . ."[138] However, the court noted that the tax commissioners testified at trial that "they [were] unaware of any way under the True Tax Value system to measure whether there is equality among the various classes of property."[139] Uniformity and equality "requires that the property tax system be based on objectively verifiable data [to ensure] that taxpayers have a means to evaluate the taxing authorities' assessment of their property."[140] After finding that uniformity and equality requires resort to objectively verifiable data, the court examined whether the use of cost schedules satisfied this requirement. As previously stated, "the cost schedules were generated by using the 1985 prices of items found in buildings reduced [15%] across the board."[141] The ISBTC regulations were the only means by which a complaining taxpayer could challenge the cost schedules. "Because the present system does not allow comparison of assessments to objective data, it cannot satisfy the constitutional requirements of uniformity and equality in property assessment."[142] Without use of objectively verifiable data, a taxpayer cannot challenge an assessment and a court has no way to review such an assessment for uniformity and equality.[143] Because the current true tax value system does not provide for uniformity and equality, as measured by reference to objectively verifiable data, the court held that the system was in violation of article X, section 1 of the Indiana Constitution.[144]

The court next addressed whether Indiana's property tax system violated Due Course of Law, article I, section 12 of the Indiana Constitution. The petitioners argued that Indiana's system lacked due process, basing their argument on the fact that in Indiana, "every person, for injury done to him in his person, property, or reputation, shall have remedy by due course of law."[145] The ISBTC countered that the "regulations provide all the process that is constitutionally due."[146] To satisfy due process, the ISBTC must use ascertainable standards in rendering a decision.[147] Not only must the regulations provide a taxpayer with the right to challenge an assessment, "they must also provide an opportunity to be heard 'in a meaningful manner.'"[148] The court examined some examples[149] and held that

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138. *Id.* at 376.

139. *Id.*

140. *Id.*

141. *Id.* at 377.

142. *Id.* at 378.

143. *See id.*

144. *Id.* at 382.

145. *Id.* at 383 (quoting IND. CONST. art. I, § 12).

146. *Id.*

147. *See id.* at 383-84 (quoting Harrington v. State Bd. of Tax Comm'rs, 525 N.E.2d 360, 361 (Ind. Tax Ct. 1988) (citations omitted)).

148. *Id.* at 384 (quoting Mathews v. Eldridge, 424 U.S. 319, 333 (1976)).

149. *Id.* at 385 (noting that in determining "neighborhood desireability," no objective standards were used); *id.* at 385-86 (noting that taxpayers have no meaningful opportunity to

"[t]he [t]rue [t]ax [v]alue system violates due process because it deprives taxpayers of their right to introduce real world, objective evidence in order to challenge assessments."[150]

The court next addressed petitioners claim that the true tax value system violated the Due Process Clause of the Fourteenth Amendment to the U.S. Constitution, procedurally and substantively. As to procedural due process, the petitioners argued that taxpayers are not provided a meaningful opportunity to respond because real world information is irrelevant according to ISBTC regulations. Therefore, procedural due process was violated because the refusal to consider such information acts as a conclusive presumption against the taxpayer.[151] The ISBTC contended that the presumption was merely a necessary substantive rule of law.[152] Finding the petitioners' argument unpersuasive, the court rejected the claim that procedural due process was violated.[153]

The petitioners next argued that the tax system violated their substantive due process rights. The petitioners claimed that because of this violation, they paid a disproportionate amount of taxes.[154] To show that one's substantive rights have been violated, the petitioners must

> demonstrate either that 1) the law infringes "fundamental rights [or] liberties which are, objectively, 'deeply rooted in this Nation's history and tradition,' and 'implicit in the concept of ordered liberty,' such that 'neither liberty nor justice would exist if they were sacrificed;'" or 2) the law is "arbitrary and unreasonable, having no substantial relation to the public health, safety, morals, or general welfare."[155]

Because the petitioners did not assert that a fundamental right was violated, the court reviewed the petitioners' claim under the arbitrary and unreasonable standard.[156] The ISBTC argued that the system results in taxpayers paying their fair share.[157] The court found that the ISBTC's action passed the rational basis test and held that petitioners failed to demonstrate a substantive due process

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challenge the determination of a neighborhood's boundaries because the ISBTC limits the use of comparison properties outside one's subdivision, as determined by the ISBTC); *id.* at 386 (finding that "there are no objective standards to determine whether an opinion of condition is correct"); *id.* (finding that in determining grade factors, particularly when an "A" grade factor is adjusted upward, there are no ascertainable standards in deciding a grade factor other than the subjective beliefs of the hearing officer); and *id.* (finding that in determining obsolescence, "there are no objective standards used for measuring obsolescence").

150. *Id.* at 388.

151. *See id.* at 389.

152. *See id.*

153. *Id.* at 390.

154. *See id.*

155. *Id.* (quoting Washington v. Glucksberg, 117 S. Ct. 2258, 2268 (1997) (citations omitted); Euclid v. Ambler Realty Co., 272 U.S. 365, 395 (1926)).

156. *Id.* at 390-91.

157. *See id.* at 391.

claim.[158]

The petitioners' last argument was that the system violated the Equal Protection Clause of the Fourteenth Amendment to the U.S. Constitution "because it is irrational and produces arbitrary results."[159] The Fourteenth Amendment states that "no state shall 'deny to any person within its jurisdiction the equal protection of the laws.'"[160] The petitioners claimed that their equal protection rights were violated because the true tax value system applies different assessment standards to different types of property. The petitioners also argued that their equal protection rights were violated because market values are not used in assessment. However, "so long as the classification is rationally related to a legitimate state interest" the system will be valid.[161] The ISBTC maintained that the "'classifications are rationally related to the legitimate governmental purposes of establishing a property taxation system that is understandable, easy to use, uniform across types of real property, and values like properties alike.'"[162] Though the system differentiates among different classes of property, the court found that this was not enough to support a claim of equal protection violation.[163] Additionally, "even though [the system] is not based on market information"[164] and because the classifications "are not [arbitrary] under a federal equal protection standard[,]"[165] the court held that the system "is constitutional on equal protection grounds . . . ."[166] Thus, the tax court found that Indiana's true tax value system did not violate the U.S. Constitution, but struck down the law as unconstitutional based on provisions in Indiana's Constitution.

2. Zakutansky v. State Board of Tax Commissioners.[167]—Zakutansky owned property located three rows off the shore of Lake Michigan. Pursuant to Indiana Code section 6-1.1-4-13.6 the county and ISBTC promulgated a land order to be used in assessing property in the county.[168] Zakutansky's land was assessed at $350 per front foot and, disagreeing with the assessment, he appealed to the County Board of Review ("CBOR"). The CBOR reduced the assessment. Still unsatisfied, Zakutansky petitioned the ISBTC. However, the ISBTC denied the protest, believing that so long as the county complied with a valid land order, a taxpayer could not protest.[169] Zakutansky alleged that the ISBTC's determination violated the requirement of a uniform and equal rate of property assessment and

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158. *Id.*
159. *Id.*
160. *Id.* (quoting U.S. CONST. amend. XIV, § 1.)
161. *Id.* (citing City of Cleburne v. Cleburne Living Ctr., 473 U.S. 432, 440 (1985))
162. *Id.* at 393 (quoting ISBTC's Trial Brief, at 17).
163. *Id.*
164. *Id.* at 396.
165. *Id.*
166. *Id.* at 397.
167. 691 N.E.2d 1365 (Ind. Tax Ct. 1998).
168. *See id.* at 1367 (citing IND. CODE § 6-1.1-4-13.6 (1998)).
169. *See id.*

taxation[170] and that an incorrect depth table was used in calculating the property's base rate.[171]

Zakutansky submitted evidence as to the valuation of similar property within the neighborhood but not within his specific subdivision.[172] The ISBTC contended that because the land order was valid and Zakutansky's property was valued consistently with other property within his subdivision, the assessment pursuant to the land order must also be valid. Therefore, the ISBTC did not consider the evidence submitted by Zakutansky in making its decision, believing that Zakutansky's only remedy was to challenge the land order. However, the court stated that the purpose of the right guaranteed by Indiana's Constitution is to protect taxpayers from governmental abuse; therefore, the court found that the ISBTC was obligated to review assessments challenged by a taxpayer.[173] Additionally, "[i]f an otherwise valid [l]and [o]rder results in an individual assessment that is not uniform and equal, the [l]and [o]rder as applied to the assessment yields to the constitution."[174] Moreover, the court determined that the ISBTC was obligated to consider surrounding properties, regardless of the subdivision involved, when assessing property.[175]

In this case, Zakutansky introduced into evidence a list of comparable property in his neighborhood, property record cards for each property, and pictures of the properties.[176] The comparable properties were assessed at rates ranging from $100 to $150 per front foot, rates significantly less than the rate used for his property. Because the ISBTC did not testify as to any of the comparable properties and having already determined that the ISBTC had an obligation to consider comparable property within the neighborhood, the court remanded the case to the ISBTC to determine the rate that was applicable to Zakutansky's property, which rate was to be the same rate that was used for comparable properties.[177]

The court next addressed whether the ISBTC used an incorrect depth table in calculating the base rate of Zakutansky's property. Zakutansky submitted evidence stating that the ISBTC did not consider any other depth factors within the neighborhood in determining the depth factor of his property and alleged that such error was arbitrary and capricious. Finding that Zakutansky bore his burden of going forward and that the hearing officer did not consider Zakutansky's evidence, the court remanded this issue to the ISBTC for a determination of the predominant lot depth of the neighborhood at issue.[178]

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170. *See id.* (citing IND. CONST. art. X, § 1(a)).

171. *See id.*

172. *See id.* at 1368.

173. *Id.*

174. *Id.* (citing IND. CODE § 1-1-2-1 (1998)).

175. *Id.* at 1369 (citing Vonnegut v. State Bd. of Tax Comm'rs, 672 N.E.2d 87, 90 (Ind. Tax Ct. 1996)).

176. *See id.*

177. *Id.* at 1370.

178. *Id.* at 1370-71.

3. Town of St. John v. State Board of Tax Commissioners ("*St. John IV*").[179]—This opinion supplements the tax court's earlier decision in *St. John III.*[180] In *St. John III*, the court determined Indiana's property tax assessment system to be unconstitutional[181] and retained jurisdiction to determine a date upon which the system must comply with the Indiana Constitution.[182] The ISBTC argued that the date of the next general reassessment, March 1, 2001, should suffice as an appropriate date upon which taxpayers may have their assessments tested against "real world values," as mandated by the court in *St. John III.*[183] The petitioners countered that the ISBTC should be required to have such a system in place within thirty days.[184] In balancing the desire to avoid creating chaos among the taxing agencies by implementing such a sweeping change immediately and the desire to protect the constitutional rights of Indiana taxpayers, the court held that the ISBTC must "consider all competent real world evidence presented to the [ISBTC] by persons filing appeals on or after May 11, 1999."[185]

4. Talesnick v. State Board of Tax Commissioners.[186]—Talesnick owned property in the Eagle Ridge subdivision off the banks of the Eagle Creek Reservoir. As compared to other subdivisions in the reservoir area, the Eagle Ridge subdivision did not have city water, sewers, fire hydrants, or city-maintained streets.[187] The ISBTC promulgated a land order, in accordance with statute, to be used by county officials in assessing property.[188] Under the land order, the base value of properties in Eagle Ridge subdivision could range between $90,000 and $110,000 for the first acre of land owned.[189] Talesnick's land was assessed at the highest amount allowed under the land order. After the CBOR denied Talesnick's request to alter the assessment, he petitioned the ISBTC for review.[190] The ISBTC denied Talesnick's protest and increased the assessed value of the home. Talesnick brought suit alleging that the land was

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179. 691 N.E.2d 1387 (Ind. Tax Ct. 1998), *clarified*, 698 N.E.2d 399 (Ind. Tax Ct. 1998), *aff'd in part, rev'd in part*, 702 N.E.2d 1034 (Ind. 1998).

180. 690 N.E.2d 370 (Ind. Tax Ct. 1997).

181. *Id.* at 398.

182. *Id.*

183. *See St. John IV*, 691 N.E.2d at 1388.

184. *See id.*

185. *Id.* at 1390. But note, this opinion was affirmed in part and reversed in part by the Indiana Supreme Court in *State Board of Tax Commissioners v. Town of St. John*, 702 N.E.2d 1034 (Ind. 1998), handed down on December 4, 1998. That case will be discussed in the *1999 Developments in Indiana Taxation* covering the period of October 1, 1998 through September 30, 1999.

186. 693 N.E.2d 657 (Ind. Tax Ct. 1998).

187. *See id.* at 658.

188. *See id.* (citing IND. CODE § 6-1.1-4-13.6 (Supp. 1997) (as amended at IND. CODE § 6-1.1-4-13.6 (1998)).

189. *See id.*

190. *See id.*

given an improper value and that an increase in value of the home was invalid because he was not given an opportunity to respond to the increase in assessment.[191]

Talesnick presented evidence that comparable properties in other subdivisions were valued at the same amount as the Talesnick's property, despite the lack of amenities (city water, sewage, and street maintenance) present on the other properties.[192] Talesnick also presented evidence that a water flowage easement encumbered more of his land than compared with other property within the subdivision; therefore, his property was assessed at a higher comparable amount than his neighbor's property.[193] Talesnick argued that the property was entitled to a negative influence factor for the property due to the lack of amenities. "A negative influence factor is justified in instances where property has a 'condition peculiar to the land that dictates an adjustment, either positive or negative, to the extended value to account for variations from the norm.'"[194] The court, citing *Vonnegut v. State Board of Tax Commissioners*,[195] remanded the case to the ISBTC because the ISBTC failed to consider any evidence of comparable properties outside Talesnick's subdivision, and ordered that the ISBTC consider comparable properties within other subdivisions when examining the assessment of Talesnick's property, taking into account the evidence presented by Talesnick.[196]

After the hearing officer inspected the property, the hearing officer increased the assessment of the home, claiming that the original assessment miscalculated the square footage of the finished basement. Talesnick argued that he was not given an opportunity to respond to the increase in assessment. The court pointed out that by statute[197] the ISBTC may raise the assessed value of property during a taxpayer initiated petition for review.[198] However, the court remanded the case to the ISBTC for a remeasurement of the basement, because there was confusion about the actual finished square footage in the basement.[199] The court did not address Talesnick's lack of opportunity to respond because it ordered the remeasurement.[200]

5. Garcia v. State Board of Tax Commissioners.[201]—The Garcias' home consisted of 10,000 square feet of living space, including an indoor swimming

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191. *See id.* at 659, 661.

192. *Id.* at 659 & n.6.

193. *Id.* at 660.

194. *Id.* (quoting IND. ADMIN. CODE tit. 50, r. 2.1-2-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-4-10(a)(9) (1996))).

195. 672 N.E.2d 87 (Ind. Tax Ct. 1996).

196. *Talesnick*, 693 N.E.2d at 660.

197. *Id.* at 661 (citing IND. CODE § 6-1.1-15-4(a) (1998)).

198. *Id.*

199. *Id.* at 662.

200. *Id.*

201. 694 N.E.2d 794 (Ind. Tax Ct. 1998).

pool with an area of 2717 square feet.[202] The home contained many amenities including cherry wood cabinets, vaulted ceilings, unusually large water and gas supply lines, and more than twenty windows on the front of the home.[203] The home was given an "A + 10" grade by the county assessor.[204] The Garcias unsuccessfully petitioned the CBOR for review of the assessment. The Garcias then petitioned the ISBTC to review the assessment. The ISBTC reduced the grade to "A + 4." Still unsatisfied with the result, the Garcias brought suit alleging that it was error to use an "A + 4" grade factor for their home and swimming pool enclosure.[205]

Indiana assesses property according to its true tax value.[206] "The [t]rue [t]ax [v]alue of a residential improvement is calculated by determining the whole dollar cost of reproducing the improvement as determined under the rules and regulations of the [ISBTC]."[207] Assessors use cost schedules to determine the base cost of reproducing a dwelling. Grade factors ranging from "A" to "E" are then used to differentiate among the quality of homes.[208] The grade factor determination is a subjective decision made by the assessor. However, ISBTC regulations define different characteristics to aid assessors in differentiating among the grades. For example, "A" grade dwellings are those having "outstanding architectural style and design and . . . are constructed with the finest quality materials and workmanship throughout."[209] "A" grade dwellings are given a grade factor of 160%; "B" grade dwellings are given a grade factor of 120%; "C" grade dwellings are given a grade factor of 100%; "D" grade dwellings are given a grade factor of 80%; and, "E" grade dwellings are given a grade factor of 60%.[210] The ISBTC also recognized that sometimes dwellings fall somewhere between the grade factors; therefore, this must be taken into account.[211] All grade factors between "A" and "E" can be given an indication of plus or minus two, or plus or minus one. This indicates that a grade falls somewhere between one of two grade letters. Also, grades falling below "E" can

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202. *See id.* at 795.

203. *See id.*

204. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1996))).

205. *Id.* at 796.

206. *Id.* (citing IND. CODE § 6-1.1-31-6 (1998)).

207. *See id.* (citing IND. ADMIN. CODE tit. 50, rs. 2.2-7-7.1, 2.2-7-9, 2.2-2-1(c) (1996)).

208. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-7-6(e) (1996)).

209. *Id.* (quoting IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1996))). "B" grade dwellings are "architecturally attractive dwellings with good quality materials and workmanship throughout." *Id.* "C" are moderately attractive with average quality of materials used; "D" are constructed with economy quality materials; and "E" are dwellings with very cheap quality of material and workmanship used. *Id.* at 796-97.

210. *See id.* at 797 (citing IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-7-6(e) (1996))).

211. *See id.*

be given a negative indication such that "E - 4" would equal 0%. Additionally, grades falling above "A" can be given an indication such that a property designated "A + 10" is priced at 360% of its base price.[212]

The problem with the true tax value system, when viewed by the court, was that an assessor was given no guidance in differentiating among an "A + 1" and an "A + 10." Thus, the court held that allowing an assessor complete autonomy and subjectivity in assessing a 200% difference in base price without providing ascertainable standards was arbitrary and capricious.[213] The court relied on *St. John III*[214] in holding that ascertainable standards are required to apprise a taxpayer of the appropriate standards that an agency will consider when making a grade factor decision, and to ensure that a reviewing court can effectively review the agency action.[215]

The Garcias next argued that the ISBTC erred in applying an "A + 4" grade factor to the swimming pool enclosure. A separate schedule is used to classify swimming pool enclosures, and this schedule classifies swimming pools as type-1, type-2, or type-3, depending upon whether the enclosure is unfinished, semi-finished, or finished, respectively.[216] A table is then applied to assign cost ranges depending on the area and type of the enclosure. However, the table only includes areas of up to 1000 and the Garcias' enclosure was 2717 square feet.[217] The hearing officer merely located the cost amount of a 1000 square foot, type-3 enclosure ($21.55 per square foot) and calculated the total value by applying an "A + 4" grade factor. The hearing officer reasoned that if the home was given an A + 4 rating, then the swimming pool enclosure should have the same factor.[218]

However, the court first noted that according to ISBTC regulation, the hearing officer should have extrapolated the average cost per square foot in reaching a value to apply to a swimming pool enclosure greater than 1000 square feet.[219] The Garcias also argued, and the court agreed, that grade factors are not to be applied to swimming pool enclosures.[220] The court compared swimming pool enclosures to cost schedules for similar improvements (gazebos, greenhouses, car sheds, etc.), with respect to which the applicable regulation specifically provided for grade factors to apply. Because the regulation under consideration did not contain a similar statement, the court held that in the absence of specific language to the contrary, grade factors were not to be applied

212. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-3-2 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-7-6(e) (1996))).

213. *Id.* at 798.

214. 690 N.E.2d 370 (Ind. Tax Ct. 1997).

215. *Garcia*, 694 N.E.2d at 796.

216. *See id.* at 798.

217. *See id.*

218. *See id.* at 798-99.

219. *Id.* at 799 (citing IND. ADMIN. CODE tit. 50, r. 2.1-3-4 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-9-3 (1996))).

220. *Id.*

to swimming pool enclosures, but rather, the extrapolated amount was to be applied to the total square footage.[221]

B. Indiana Property Taxes—Business Real Property Taxes

1. Wareco Enterprises, Inc. v. State Board of Tax Commissioners.[222]—Wareco appealed the ISBTC's final determination of a real property assessment by filing a Form 133 Petition for Correction of Errors. Wareco alleged that there was an error in calculating the perimeter to area ratio ("PAR"), an error in the base rate calculations, and an error in the use of the depreciation tables.[223] A hearing officer was assigned to review the petition and made recommendations to the ISBTC to correct errors. Despite the recommendations, the ISBTC issued a final determination claiming that either the assessments were correct or that the errors could not be corrected using Form 133.[224] The court found that because the hearing officer supplied ample evidence to show that the assessments were incorrect, the only issue remaining was whether Form 133 is the necessary form to correct such errors. The court has "held that '[t]he only errors subject to correction by a Form 133 are those which can be corrected without resort to subjective judgment.'"[225]

The PAR is used to calculate the total square foot area of a building. The applicable regulations state that adjustments to the PAR should be made to reflect variations in use or wall height.[226] The court noted that according to the regulations, it is only necessary to measure the exterior walls in order to calculate the PAR and the court determined that these were objective measurements.[227] The ISBTC claimed that PAR is a subjective determination and not correctable by filing a Form 133 Petition for Correction of Errors. The court held that, even though the hearing officer used a different method of calculating PAR than did the county board, the calculation of PAR under either method is objective and therefore correctable using Form 133.[228]

Wareco next argued that the base rate was incorrectly calculated. The ISBTC again reiterated the ISBTC's position that the base rate calculation is a subjective determination that cannot be corrected with Form 133. Models are used to establish the base rate of a building presumed to have the same interior and mechanical components as the model.[229] The regulations provide schedules

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221. *Id.* at 800.

222. 689 N.E.2d 1299 (Ind. Tax Ct. 1997).

223. *See id.* at 1299-1300.

224. *See id.* at 1300.

225. *Id.* at 1301 n.2 (quoting Bock Prod., Inc. v. State Bd. of Tax Comm'rs, 683 N.E.2d 1368, 1372 (Ind. Tax Ct. 1997)).

226. *See id.* at 1301 (citing IND. ADMIN. CODE tit. 50, r. 2.1-4-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-2 (1996))).

227. *Id.*

228. *Id.*

229. *See id.* at 1302 (citing IND. ADMIN. CODE tit. 50, r. 2.1-4-3 (1992) (recodified at IND.

showing the costs of components that are used to adjust for variations.[230] The hearing officer testified that there was no heat in portions of the building and that the building did not have a partition wall as presumed by the model.[231] Additionally, the hearing officer testified that a mistake in calculating the PAR would result in an error in calculating the base rate.[232] Finding that the base rate calculation is an "uncomplicated" determination not requiring subjective judgment, and correctable using Form 133, the court held that it was arbitrary and capricious not to do so.[233]

The court next addressed Wareco's claim that an incorrect depreciation life was used. The ISBTC applied a forty-year life to the building as opposed to a thirty-year life. Applying the regulations, a light pre-engineered building has a thirty-year life and all fire resistant buildings not listed elsewhere in the regulation have a forty-year life.[234] The testimony of the hearing officer established that the building was a light pre-engineered building; therefore, subject to a thirty-year life. The court held that no subjective determination was required to find that the building has a thirty-year life under the tables provided in the regulation and, therefore, correction using Form 133 was appropriate.[235]

2. Indianapolis Historic Partners v. State Board of Tax Commissioners.[236]—Indianapolis Historic Partners ("IHP") owned a three-story apartment building known as "The McKay." In 1989, the ISBTC established a county land valuation commission in each county;[237] the commission was given the power to determine the value of land in its own county.[238] The Marion County commission adopted schedules that provide acreage values for both apartment land and commercial land. The schedules place maximum limits upon which an acre of apartment or commercial land can be valued. The apartment land schedule also established criteria for which the land should be valued according to very good, good, average, fair, or poor standards.[239] The ISBTC subsequently approved the county order.[240]

During the 1989 assessment, The McKay was assessed at a value per square foot using the commercial land schedule instead of the apartment land schedule. IHP brought suit alleging that the ISBTC applied the incorrect schedule.[241] The

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ADMIN. CODE tit. 50, r. 2.2-10-6.1 (1996))).

230. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-4-3 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-6.1 (1996))).

231. *See id.*

232. *See id.*

233. *Id.*

234. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-5-1 (1992) (repealed)).

235. *Id.* at 1302-03.

236. 694 N.E.2d 1224 (Ind. Tax Ct. 1998).

237. *See id.* at 1225 (citing IND. CODE ANN. § 6-1.1-4-13.6 (West 1989 & Supp. 1997)).

238. *See id.*

239. *See id.* at 1225 n.1.

240. *See id.* at 1225.

241. *See id.* at 1226.

ISBTC contended that it could use the commercial land schedule to value The McKay. The ISBTC set forth several reasons for this contention including that the building: was located in an urban area; was on a small parcel of land; was on platted land; and, did not have amenities, such as, a pool or wooded rolling hills (as set forth in the schedule as characteristics to look for when determining whether the land is good, very good, average, etc.).[242] At trial, the ISBTC also contended that because the property was on land of less than one acre, the ISBTC could use the commercial land schedule to value the property.

The court found that the plain language of the county order in classifying the schedule as "Apartment Land" mandated that the schedule would apply to all land upon which an apartment is situated.[243] In holding that use of the commercial land schedule for apartment buildings was erroneous, the court sarcastically stated that "[a] contention that land being used for industrial purposes should be assessed using the rural residential schedule of the Land Valuation Order would never be allowed to stand [and] [n]either should a contention that land upon which apartments have been constructed should be assessed using commercial values . . . ."[244] The ISBTC made the following three arguments to demonstrate that it was entitled to use the commercial land schedule in valuing The McKay: The county order was to be applied as written; IHP cannot challenge the values in the order; and, as the assessing expert, the ISBTC's decision should control.[245]

As to the ISBTC's first argument, the court merely reiterated that according to the plain language of the county order, the ISBTC was applying the order as written by disallowing use of the commercial land schedule for apartment land.[246] As to the second argument, the court pointed out that IHP was not challenging the values underlying the order, but rather, arguing that the schedules were improperly applied.[247] As to ISBTC's third argument, the court merely stated that "[t]he State Board has presented no expertise here. Expertise is demonstrated by expert action, not a will to power."[248]

After determining that use of the commercial land schedule was error, the court addressed whether the assessment violated the requirement of uniformity and equality in assessment as guaranteed by the Indiana Constitution.[249] The court stated that "[l]and [o]rders have the force of law and are to be complied with as long as the applied [l]and [o]rder results in constitutional assessments."[250] In the absence of evidence demonstrating that The McKay was functionally distinct from other land upon which apartments are located, the court held that

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242. *See id.*
243. *Id.* at 1227.
244. *Id.*
245. *See id.*
246. *Id.*
247. *Id.*
248. *Id.* at 1228.
249. *Id.* (citing IND. CONST. art. X, §1).
250. *Id.* at 1229.

the use of the commercial land schedule violated the mandates of the Indiana Constitution.[251]

3. Dana Corp. v. State Board of Tax Commissioners.[252]—Dana challenged the ISBTC's final determination of the assessment of Dana's property and moved for summary judgment. Dana contended that any property assessment made pursuant to ISBTC regulations is arbitrary, capricious, and an abuse of discretion because the regulations provide no ascertainable standards upon which a taxpayer would know or a court could review such a decision.[253] The ISBTC maintained, and the court agreed, that Dana had merely attempted to enjoy retroactive effect of the court's holding in *St. John III*.[254] In *St. John III*, the court limited its holding to all assessments and appeals made on or after May 11, 1999. After that date, a taxpayer can facially challenge the property tax assessment system as unconstitutional, using *St. John III* in support of such claim.[255]

However, the court recognized that it would continue to entertain "as applied" challenges to the current system.[256] The court then turned to whether Dana had supplied sufficient evidence to warrant summary judgment for an as applied challenge. Finding that Dana had not supplied any evidence to demonstrate that no genuine issue of material fact exists, the court denied the motion for summary judgment.[257]

4. Wetzel Enterprises, Inc. v. State Board of Tax Commissioners.[258]—Wetzel owned .4 acres of land and improvements made upon the land. During the 1989 general reassessment, Wetzel's property was increased in value over the previous reassessment. Wetzel did not appeal the assessment; however, a county assessor did file a petition for review with the Vanderburgh CBOR. In 1991, the CBOR reduced the assessed value, retroactive to 1989.[259] Eight months after the CBOR's decision, the same county assessor filed a petition for review with the ISBTC. Wetzel did not receive notice of a hearing on the matter.[260] Subsequently, on February 23, 1996, the ISBTC issued its final determination of assessment, invalidating the CBOR's reduction.[261]

The ISBTC argued that only a specific taxpayer can file a petition for review with the CBOR and that any action taken by the CBOR with respect to Wetzel's property was invalid. The court pointed out that the relevant statute included language such that a CBOR could review an assessment brought to its attention by "any person" and that filing a petition for review was a way for "any person"

251. *Id.* at 1230.
252. 694 N.E.2d 1244 (Ind. Tax Ct. 1998).
253. *See id.* at 1246.
254. 690 N.E.2d 370 (Ind. Tax Ct. 1997).
255. *See Dana*, 694 N.E.2d at 1247.
256. *Id.*
257. *Id.* at 1248.
258. 694 N.E.2d 1259 (Ind. Tax Ct. 1998).
259. *See id.* at 1260.
260. *See id.* at 1261.
261. *See id.*

to bring an assessment to the CBOR's attention.[262] However, the court believed that the issue of the case was whether the ISBTC could review the CBOR's assessment more than four years after Wetzel received and paid the reduced tax bills.[263]

There are two ways in which the ISBTC can review an assessment: (1) when a taxpayer files a petition for review, or (2) where the ISBTC decides to sua sponte review an assessment.[264] In this case, a petition was filed. However, a petition must be filed within thirty days after the CBOR's determination.[265] Here, the petition was filed eight months after the CBOR's final determination. In limited circumstances, the ISBTC can review untimely filed petitions.[266] In any event, whether by petition or sua sponte, the ISBTC can only alter assessments if done so within three years after the assessment was made.[267] In this case, the ISBTC attempted to alter an assessment made four years prior. Even if the ISBTC could establish that it could review the assessment sua sponte, it failed to provide Wetzel with proper notice and a hearing. Therefore, the court held that the ISBTC could not alter the CBOR's reduction in value.[268]

5. Zakutansky v. State Board of Tax Commissioners.[269]—Zakutansky owned a marina consisting of land, several pole barns, and a series of docks. The property was assessed and Zakutansky sought review of the assessment. Still unsatisfied with the determination on review, Zakutansky appealed the decision, making three claims of error.[270]

First, Zakutansky argued that a sloped retaining wall was incorrectly assessed. The wall had been valued by the assessor using a per-square-foot basis rather than a per-linear basis, as required by regulation.[271] Though the ISBTC agreed to correct the mistake, the ISBTC maintained that an "A" grade factor was appropriate. Grade factors are used to differentiate among properties because of quality of materials and workmanship.[272] Zakutansky offered evidence tending to show that an "A" grade was not appropriate. The evidence proffered showed that the wall was deteriorating, there were no footings or metal rods supporting the concrete and the cost of building a similar wall was substantially less than the

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262. *Id.* at 1261 n.5 (citing IND. CODE § 6-1.1-13-5 (1998)).

263. *Id.* at 1261.

264. *See id.* at 1261-62 (citing IND. CODE § 6-1.1-15-3 (1998); IND. CODE 6-1.1-14-10 (1998)).

265. *See id.* at 1262 (citing IND. CODE § 6-1.1-15-3 (1998)).

266. *See id.* (citing State Bd. of Tax Comm'rs v. New Energy Co. of Indiana, 585 N.E.2d 38, 39 (Ind. Ct. App. 1992) (holding that the ISBTC may consider untimely filed applications for deductions)).

267. *See id.* (citing IND. CODE §§ 6-1.1-9-4, 6-1.1-14-11 (1998)).

268. *Id.* at 1263.

269. 696 N.E.2d 494 (Ind. Tax Ct. 1998).

270. *See id.* at 495.

271. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-4-5 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-12-5 (1996))).

272. *See id.* at 495 n.1.

value assigned by the ISBTC. Because Indiana's tax system is not based on fair market value, however, the court stated that evidence of reproduction cost is not determinative (though it is probative of the quality of materials and workmanship).[273] Even though the evidence of reproduction cost was not dispositive, the ISBTC was still required to support its finding of an "A" grade with substantial evidence. The court held that the ISBTC had not presented substantial evidence justifying an "A" grade other than the unsupported subjective opinions of the hearing officer and remanded the issue to the ISBTC.[274]

Zakutansky next argued that the ISBTC used an incorrect schedule in valuing the pole barns located on the land. The ISBTC used the general commercial-mercantile cost schedule rather than the agricultural schedule.[275] The ISBTC contended that the ISBTC used the appropriate schedule due to the use of the barns by Zakutansky. The court held that actual use of the property is not dispositive; but rather, physical features are used to determine which schedule is to be used.[276] Thus, the court held that the schedule for agricultural pole barns was to be used in this case.[277]

Zakutansky's third argument was that the ISBTC improperly assessed the land. Zakutansky claimed that the land was subjected to a restrictive easement preventing construction on portions of the land. Furthermore, the only utility servicing the land was electricity.[278] Zakutansky then presented evidence of comparable properties that were assessed at a lesser rate than his. The ISBTC had not considered the other properties when making its determination. Therefore, the court held that the ISBTC was required to consider such comparable properties and remanded the issue to the ISBTC.[279]

6. King Industrial Corp. v. Indiana State Board of Tax Commissioners.[280]—King, a tool and die manufacturer, used four buildings in its operations. The buildings were assessed in 1993.[281] King filed a petition for review with the CBOR, which did not change the assessment. King then filed petition for review with the ISBTC, claiming that King was entitled to a kit adjustment. The ISBTC denied the adjustment and King appealed.[282]

The ISBTC has provided for a 50% reduction in base price for "kit"

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273. *Id.* at 496.

274. *Id.*

275. *See id.*

276. *Id.* at 497 (citing Herb v. State Bd. of Tax Comm'rs, 656 N.E.2d 890, 893 (Ind. Tax Ct. 1995)).

277. *Id.*

278. *See id.*

279. *Id.* at 498 (citing Talesnick v. State Bd. of Tax Comm'rs, 693 N.E.2d 657 (Ind. Tax Ct. 1998)).

280. 699 N.E.2d 338 (Ind. Tax Ct. 1998).

281. *See id.* at 339.

282. *Id.*

buildings (i.e., light pre-engineered buildings).[283] Kit buildings are made of light weight and inexpensive materials and come pre-fabricated such that they can be assembled like a kit.[284] To clarify what was intended to qualify for a kit adjustment, the ISBTC published Instructional Bulletin 91-8. The bulletin contained several examples of kit characteristics.[285] Though the bulletin was intended to clarify the definition of a kit building, the court believed that it made such a determination more confusing than before due to the use of vague terminology that left many decisions to the subjective discretion of the assessors.[286] The bulletin also discussed using grade factors in conjunction with the kit adjustment. Thus, a building could be given a 50% reduction as qualifying for the kit adjustment and then adjusted upward for additional amenities, or a building could be denied a kit adjustment and then adjusted downward to reflect a lack of amenities.[287] Either way the determination was intended to compute the building's true tax value.[288]

King argued that it was entitled to the 50% adjustment because its buildings contained at least ten of the characteristics listed in the bulletin. To the contrary, the ISBTC argued that King was not entitled to the adjustment because the buildings did not satisfy several of the other characteristics contained in the bulletin. However, the court pointed out that none of the characteristics noted by the ISBTC absolutely disqualified the buildings from receiving the kit adjustment and stated that "a building may still qualify for the kit adjustment even though it contains minor enhancements."[289] King also argued that the ISBTC applied an incorrect grade factor ("D + 1") to its buildings. Based on this information, the court found that the ISBTC had in no way supported its determination that a grade factor of "D + 1" should be used as opposed to any other grade factor.[290] In light of the fact that the hearing officer testified that he may have made a mistake, the court remanded the issue to the ISBTC, holding that the ISBTC had acted arbitrarily and capriciously and that its determination was unsupported by substantial evidence.[291]

7. Barth, Inc. v. State Board of Tax Commissioners.[292]—Barth owned two parcels of land upon which four buildings are constructed. Barth filed a Form 133 Petition for Correction of Error for the assessed value of its property for the tax years 1989 through 1991.[293] The petition was subsequently denied by both

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283. *See id.*
284. *See id.*
285. *See id.*
286. *Id.*
287. *See id.* at 341.
288. *See id.*
289. *Id.* at 342 (citing Componx, Inc. v. State Bd. of Tax Comm'rs, 683 N.E.2d 1372, 1375 (Ind. Tax Ct. 1997)).
290. *Id.*
291. *Id.* at 343.
292. 699 N.E.2d 800 (Ind. Tax Ct. 1998).
293. *See id.* at 801.

the county auditor and the ISBTC. Thereafter, Barth appealed to the court, claiming that the base rates used were incorrect, that the buildings were entitled to a kit adjustment for 1991, and that two of the buildings should have been depreciated using a thirty-year rather than a forty-year life expectancy table.[294]

Form 133 petitions can be filed to correct only objective errors.[295] Thus, only in cases where error can be corrected without resorting to subjective judgment can a taxpayer use Form 133.[296] The ISBTC argued that any changes in the base rate would be subjective in nature and could not be corrected using Form 133. However, it is incumbent upon the ISBTC to investigate a taxpayer's claim in order to determine whether the taxpayer is challenging objective or subjective determinations.[297] The ISBTC failed to investigate the allegations, therefore the court discussed Barth's arguments. Base rate is a factor used in calculating the reproduction cost of an improvement.[298] Base rates are calculated by first selecting the model most representative of the physical characteristics of the improvement at issue and then second, applying the pricing schedule to adjust for additional or non-existent components or amenities.[299] A model presumes that many components exist within the subject improvement in setting a property's value. If any components are absent or if any additional amenities exist, the schedule assigns a cost to be deducted or added to the model's base rate.[300] In this case, Barth argued that its buildings lacked many of the components presumed to be included in the model, such as a lack of partitioning and a lack of interior finish. As to whether these errors, if any, could be corrected using a Form 133 depends upon the nature of the features that are not present. For example, when the pricing schedule lists a cost for the feature alleged not to be present, it results in a simple observation of fact without resort to subjective judgment.[301] The court remanded this issue to the ISBTC because the ISBTC had failed to consider whether the base rate was correctable using a Form 133.[302]

The court next addressed Barth's contention that it was entitled to a kit adjustment. Subject to ISBTC regulations, kit buildings are entitled to a 50% reduction in base rate. By order, the ISBTC required all county assessors to reassess all improvements entitled to the 50% reduction. However, the county assessor did not grant Barth a kit adjustment and this was claimed as error. By bulletin, the ISBTC instructed taxpayers challenging the denial of a kit

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294. *See id.*

295. *See id.* at 802.

296. *See id.* (citing Bock Prod., Inc. v. State Bd. of Tax Comm'rs, 683 N.E.2d 1368, 1370 (Ind. Tax Ct. 1997)).

297. *See id.* at 803 n.6 (citing Wareco Enter. v. State Bd. of Tax Comm'rs, 689 N.E.2d 1299, 1302 (Ind. Tax Ct. 1997)).

298. *See id.* at 802.

299. *See id.*

300. *See id.*

301. *See id.* at 803 (citing *Wareco Enter.*, 689 N.E.2d at 1302).

302. *Id.*

adjustment to file a Form 133.[303] At the administrative level, the ISBTC found no error in the assessment because two of the buildings were given a grade factor of "D" and the other two were given a grade of "C - 2."[304] The ISBTC believed that instead of receiving the kit adjustment, the buildings were given a lower grade which already compensated for the denial of the adjustment; therefore, the ISBTC did not reach the issue of whether the buildings were entitled to the kit adjustment in the first place. However, the court held that the "plain language of the regulation admits of no exceptions and requires [that] the kit adjustment [] be given where the building qualifies for the adjustment, whether local assessing officials have previously decided to give the building a lower grade or not."[305] Because the ISBTC failed to consider whether Barth was entitled to the kit adjustment, the court remanded the issue to the ISBTC. If on remand the ISBTC determines that Barth is entitled to the kit adjustment, the ISBTC would be allowed to adjust the grade factors to prevent a windfall in favor of Barth even though, generally, the ISBTC cannot make subjective corrections with respect to a Form 133.[306]

Finally, Barth argued that two of the buildings should have been depreciated using a thirty-year rather than a forty-year life expectancy table. The ISBTC countered that to correct the error, if any, would require subjective judgment and therefore it need not consider Barth's argument. However, the court reiterated that the ISBTC has a duty to investigate a taxpayer's claim in order to determine whether the taxpayer is challenging objective or subjective determinations.[307] Light pre-engineered buildings are depreciated using a thirty-year life expectancy table and all fire-resistant buildings, not listed elsewhere in the regulations, are depreciated using a forty-year life expectancy table.[308] Thus, the court believed that the real issue was whether the buildings were classified as "light pre-engineered."[309] Because Barth used Form 133, only objective errors can be corrected. Objective errors are those that require an uncomplicated (or straight forward true or false) application of the regulations. Thus, if on remand the ISBTC determines that the buildings are entitled to a kit adjustment, then the buildings should be depreciated using the thirty-year table because kit buildings are by definition light pre-engineered buildings. However, if on remand it is determined that the buildings are not entitled to the kit adjustment, then there would be a factual question as to whether the buildings are in fact light pre-engineered, which would require resort to subjective judgment; therefore, the fact could not be correctable using Form 133.[310]

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303. *See id.* at 804 n.10 (citing Instructional Bulletin 92-1).

304. *See id.* at 804.

305. *Id.* (citations omitted).

306. *See id.* at 807.

307. *Id.* at 805-06.

308. *See id.* at 808 (citing IND. ADMIN. CODE tit. 50, r. 2.1-5-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-7 (1996))).

309. *Id.*

310. *See id.*

C. *Indiana Real Property—Business Real Property Taxes ("Obsolescence Adjustment")*

1. North Park Cinemas, Inc. v. State Board of Tax Commissioners.[311]—After the 1989 general assessment, North Park Cinemas ("North Park") petitioned the CBOR for an obsolescence depreciation adjustment, which was granted. However, Musgrave, a member of the CBOR, petitioned the ISBTC seeking review of the CBOR's determination. At the hearing, Musgrave merely stated that North Park was not entitled to the adjustment.[312] North Park did not appear at the hearing, but a county deputy assessor did appear and presented evidence that adjustments had been given to other businesses in the area. A hearing officer was assigned to the case, who inspected the property and spoke with the owner of North Park.[313] The hearing officer gave North Park an opportunity at that time to present additional evidence as to why North Park was entitled to the adjustment, but North Park did not do so. Four years later, the ISBTC issued a final determination stating that North Park was not entitled to the adjustment.[314] North Park appealed, claiming that neither Musgrave nor the ISBTC presented sufficient evidence to satisfy their respective burdens of proof. North Park also alleged that the ISBTC's final determination was arbitrary, capricious, and unsupported by substantial evidence, and in any event, that the denial of the adjustment violated the Indiana Constitution.[315]

The court first addressed the admissibility of evidence not submitted to the ISBTC. North Park attempted to introduce property cards into evidence at trial to show that other theaters within the area had received obsolescence adjustments. However, the court, relying on *State Board of Tax Commissioners v. Gatling Gun Club, Inc.*,[316] held that the trial court can only consider evidence that was presented to the ISBTC.[317]

North Park then argued that Musgrave failed to satisfy her burden of proof when she challenged the CBOR's determination. A member of a CBOR, by statute, may challenge the CBOR's determination.[318] However, the court found that Musgrave, as a board member, did not bear the burden of proof, and that a hearing officer does not owe a duty to make a case for a party,[319] but instead, it is the affirmative duty of a property owner to present evidence on its own behalf to support a claim of an obsolescence depreciation adjustment.[320]

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311. 689 N.E.2d 765 (Ind. Tax Ct. 1997).
312. *See id.* at 767.
313. *See id.*
314. *See id.*
315. *See id.* at 767-68.
316. 420 N.E.2d 1324 (Ind. Ct. App. 1981).
317. *North Park*, 689 N.E.2d at 768.
318. *See id.* at 766 (citing IND. CODE ANN. § 6-1.1-15-3(b) (1998)).
319. *Id.* at 769.
320. *Id.*

Next, the tax court addressed whether the ISBTC failed on its burden of proof. The court gave little merit to this argument, stating that a party appealing an adverse administrative decision bears the burden of proof.[321]

North Park also argued that the ISBTC's final determination was arbitrary, capricious, and unsupported by substantial evidence. However, the court relied on the following evidence in making its own decision: Musgrave presented evidence to the ISBTC that Musgrave believed North Park was not entitled to the depreciation adjustment. The deputy county assessor, acting on behalf of North Park, made only a bare assertion that the theater business is seasonal and therefore entitled to the adjustment received by other seasonal businesses.[322] The hearing officer then examined the property, discussed the findings with the owner of North Park, and gave North Park ten days to respond with additional evidence. North Park failed to respond and four years later a final determination was issued.[323] Based on these facts, the court concluded that the ISBTC's final determination was not arbitrary and capricious or unsupported by substantial evidence.[324]

Finally, the court addressed North Park's contention that the denial of the obsolescence depreciation adjustment violated "the requirement of a uniform and equal rate of property assessment and taxation."[325] North Park attempted to show that, because other theaters within the area had received an adjustment, North Park was also entitled to an adjustment. The ISBTC argued that it was not required to compare similar properties in making an assessment. The court recognized that the ISBTC is required to assess similar properties consistently and that the property record cards can be used to establish that the ISBTC did not follow the mandate of the Indiana Constitution.[326] However, because North Park failed to present this evidence at the administrative level, the court reaffirmed that North Park was not entitled to use such evidence in court.[327] The most important aspect of this case is that a party subject to a Petition for Review, even if instituted by a third party, must present evidence before the ISBTC in order to preserve potential error on appeal to the tax court.

2. Canal Square Limited Partnership v. State Board of Tax Commissioners.[328]—In this case, Canal Square owned land with apartment buildings constructed on the land. In 1991, the apartments were assessed as new construction and Canal Square petitioned for review with the CBOR.[329] The CBOR decreased the valuation. Still unsatisfied, Canal Square petitioned for

321. *Id.* at 770 (citing Meridian Hills Country Club v. State Bd. of Tax Comm'rs, 512 N.E.2d 911, 913 (Ind. Tax Ct. 1987)).

322. *See id.*

323. *See id.* at 771.

324. *Id.*

325. *Id.* (citing IND. CONST. art. X, § 1(a)).

326. *Id.*

327. *Id.* at 771-72.

328. 694 N.E.2d 801 (Ind. Tax Ct. 1998).

329. *See id.* at 802.

review with the ISBTC.[330] The ISBTC held a hearing and entered a final determination, decreasing the valuation due to an obsolescence adjustment. At the hearing, an expert witness testified on behalf of Canal Square. The expert testified that using recognized appraisal principles and based on a study compiled by the expert, the functional and economic obsolescence affecting the property equaled 34.35%. The expert concluded that because of this evidence, Canal Square was entitled to an obsolescence adjustment of 34.35%.[331] However, the ISBTC allowed an obsolescence adjustment of only 10%. Canal Square appealed the ISBTC's final determination, disputing the obsolescence adjustment and the amount of value assigned to the apartment land.

In general, if a taxpayer establishes a prima facie case of obsolescence, then the ISBTC must rebut the evidence or at a minimum enter conclusions or findings supporting a different result or the ISBTC's final determination will be reversed.[332] Thus, the court evaluated the sufficiency of evidence presented by Canal Square. In arriving at the conclusion that Canal Square was entitled to a 34.35% obsolescence adjustment, the expert testified that he used three approaches for valuing the apartment property: the income capitalization approach; the comparable sales approach; and the cost approach.[333] Using these three approaches, different market values were calculated. The expert reconciled the difference between the market values and reached a final estimate of $10,600,000.[334] In accordance with ISBTC regulations, the expert then estimated obsolescence under the cost approach.[335] The expert identified several sources of obsolescence, "including a narrow floor plan, excessive construction features required to meet the City of Indianapolis' Canal Corridor Design Guidelines, and the presence of an electrical power substation on the property site."[336] The expert then quantified the effect of the sources in arriving at an obsolescence amount and concluded that the difference between the replacement cost value (after depreciation) and the value as determined by the income capitalization and comparable sales methods was attributable to obsolescence.[337] The court agreed that such an approach could be used in calculating obsolescence.[338]

Having found that Canal Square submitted sufficient evidence to establish a prima facie case of obsolescence level, the court next addressed whether the ISBTC rebutted the evidence. The court found that the ISBTC did not provide any evidence to support its determination that Canal Square was only entitled to

330. *See id.*

331. *See id.* at 803.

332. *See id.* at 805.

333. *See id.*

334. *See id.*

335. *Id.* at 806 (citing IND. ADMIN. CODE tit. 50, r. 2.1-5-1 (1996)).

336. *Id.*

337. *See id.*

338. *Id.* at 807 (citing Thorntown Tel. Co. v. State Bd. of Tax Comm'rs, 588 N.E.2d 613, 619 (Ind. Tax Ct. 1994)).

a 10% obsolescence adjustment.[339] In its final determination, the ISBTC did not even discuss or attempt to dispute the validity of the expert's testimony. The court pointed out the hearing officer's testimony in which the expert stated that he based his opinion merely on twenty-three years of experience.[340] The court, citing *Western Select Properties v. State Board of Tax Commissioners*,[341] found that 10% was chosen based upon the subjective belief of the hearing officer, and for no other reason, and held that this required reversal.[342]

Finally, the tax court discussed whether the ISBTC applied an incorrect value to Canal Square's land. The court remanded the determination of the amount to the ISBTC for calculation in accordance with the county land order.[343]

3. Clark v. State Board of Tax Commissioners.[344]—Clark, an owner of two apartment buildings (Wood and Salisbury), filed a petition for review of the real property assessment with the CBOR. The CBOR did not change the assessment and Clark petitioned the ISBTC, which reduced the assessed value. Still unsatisfied, Clark appealed to the tax court claiming that an improper amount of obsolescence depreciation was applied.[345] The court discussed the arguments made with respect to each property separately.

a. The Wood property.—With respect to the Wood property, Clark argued that a "C" grade factor was inappropriate. A "C" grade building is constructed of average quality materials and workmanship and is in conformity with all features of the model used in the pricing schedule. The property was assessed using a general commercial residential ("GCR") pricing schedule for apartment buildings. This schedule presumes that the buildings have concrete back-up walls[346] and Clark's property did not have concrete back-up walls. However, just because a building does not contain all the features of the model does not mandate that the building be given a grade less than "C."[347] A "C" grade may still be appropriate if the building contains other features, such as higher quality materials, to make up for the lack of a feature listed in the pricing schedule.

The court found that Clark established a prima facie case of error, and thus the burden was shifted to the ISBTC to show why a "C" grade was appropriate.[348] This could be accomplished by showing the existence of the other features that were not considered in the model. The ISBTC asserted that the Wood property possessed other features, such as nice brickwork, and argued that this was sufficient to support the ISBTC's burden of proof.[349] The ISBTC pointed to the

339. *Id.*
340. *Id.* at 808.
341. 639 N.E.2d 1068, 1073 (Ind. Tax Ct. 1994).
342. *Canal Square*, 694 N.E.2d at 808.
343. *Id.* at 810.
344. 694 N.E.2d 1230 (Ind. Tax Ct. 1998).
345. *See id.* at 1233.
346. *See id.* at 1235.
347. *See id.* at 1236.
348. *Id.*
349. *See id.* at 1237.

hearing officer's conclusion that the "pluses and minuses" balanced each other out and therefore a "C" grade was appropriate. However, the court noted that the ISBTC's findings must be supported by substantial evidence.[350] Finding that there was no substantive evidence describing the particular "pluses and minuses" to determine whether the pluses outweighed or equaled the minuses, other than the mere conclusory statement, the court held that the ISBTC failed to bear its burden and remanded the issue to the ISBTC for further consideration.[351]

Clark next argued that the obsolescence depreciation adjustment of 5% was inadequate. The term "obsolescence" is defined as functional (caused by internal factors) loss of value or economic (caused by external factors) loss of value. Clark proffered maintenance records indicating excessive costs due to the fact that Clark catered to students. Clark also pointed out a lack of parking spaces, lack of an elevator, and building code violations.[352] In rendering a decision on obsolescence, an assessor must identify the causes of the obsolescence, and in addition, quantify the amount of obsolescence.[353] The court determined that because Clark established a prima facie case that other factors, not considered by the ISBTC, contributed to obsolescence, the burden of proof shifted to the ISBTC. However, the court also determined that the ISBTC rebutted the prima facie case by recognizing that the property experienced a high occupancy rate.[354] By rebutting the evidence, the burden shifted back to Clark to show that even though the occupancy rate was high, obsolescence was still justified.[355] For example, Clark might have demonstrated that Clark had to reduce rent in order to maintain the high occupancy rate. Because Clark failed to do this, the challenge on this basis failed.[356]

Clark also argued that the determination of a 5% obsolescence adjustment, as opposed to some other quantity, by the ISBTC was unsupported by substantial evidence. When the hearing officer was asked why she used 5%, as opposed to 10%, the hearing officer merely stated that it was in her discretion to select an amount of obsolescence.[357] The court agreed with Clark and determined that the amount of obsolescence was not supported by substantial evidence.[358] In its final determination, the ISBTC referenced no substantive or factual evidence indicating that 5% was chosen based on anything other than the subjective judgment of the hearing officer. Therefore, the court remanded this issue to the ISBTC for further consideration.

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350. *Id.* at 1237-38 (citing Talesnick v. State Bd. of Tax Comm'rs, 693 N.E.2d 657, 661-62 (Ind. Tax Ct. 1998); Thorntown Tel. Co. v. State Bd. of Tax Comm'rs, 629 N.E.2d 962, 965 (Ind. Tax Ct. 1994)).

351. *Id.* at 1238.

352. *See id.*

353. *See id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-5-1 (1996)).

354. *Id.* at 1239.

355. *See id.*

356. *See id.*

357. *See id.* at 1240.

358. *Id.*

The court voiced its disgust with the current process when evaluating obsolescence depreciation adjustments.[359] Taxpayers were given two avenues for attacking an obsolescence determination. A taxpayer could present evidence of other causes of obsolescence not considered by the ISBTC or demonstrate that the ISBTC's decision was not supported with substantial evidence. In the court's view, the taxpayer was allowed to present a "half-hearted" case of obsolescence and still secure reversal of a final determination.[360] To ameliorate this perceived problem, the tax court

> will not consider taxpayer complaints concerning obsolescence in cases where the [ISBTC] holds a hearing concerning an assessment (whether on a Form 131 Petition or otherwise) after the date of this opinion [April 24, 1998], unless the taxpayer has identified the causes of the alleged obsolescence and presented probative evidence that would support a quantification of obsolescence at the administrative level.[361]

The court discussed the way in which a taxpayer could satisfy this burden.[362] This was a bold step by the court in an attempt to make judicial review more efficient.

b. The Salisbury property.—The Salisbury property was given a "C" grade factor. Clark argued that a "C" grade was inappropriate because there were no concrete back-up walls, as presumed by the pricing schedule, on any floors other than in the basement. This was a sufficient showing to establish a prima facie case, which shifted the burden to the ISBTC. Finding that the ISBTC failed to overcome this burden, the court reversed the final determination and remanded the issue to the ISBTC.[363]

The Salisbury property was awarded a 5% obsolescence adjustment. Clark proffered similar evidence of obsolescence as he did for the Wood property (i.e., lack of an elevator, building code violations, and high maintenance costs), which the court determined was sufficient to establish a prima facie case and shift its burden of proof to the ISBTC.[364] The court again found that the ISBTC satisfied its burden of proof by considering the high occupancy rate of the property. The burden then shifted back to Clark who failed to proffer additional evidence. However, as with the Wood property, the court held that the ISBTC's determination of a 5% adjustment lacked a sufficient evidentiary basis and remanded this issue to the ISBTC.[365]

Finally, Clark argued that the ISBTC erred in applying the general commercial mercantile ("GCM") pricing schedule rather than the GCR schedule.

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359. *Id.* at 1241.

360. *Id.*

361. *Id.*

362. *Id.* at 1242 n.18.

363. *Id.* at 1243.

364. *Id.* (citing GTE N., Inc. v. State Bd. of Tax Comm'rs, 634 N.E.2d 882, 887 (Ind. Tax Ct. 1994)).

365. *Id.*

Clark argued that under ISBTC regulations, the property had only three stories instead of four and was subject to the GCR schedule. The GCM schedule only applies to apartment buildings with four or more stories.[366] Clark's argument rests on the contention that the basement floor is not considered in determining how many stories an apartment building contains. If the basement floor were not included, there would only be three stories and the GCR schedule would be applicable. However, the court pointed out that "basement" was defined by regulation as a "story" and held that the basement could be included when determining which pricing schedule to apply.[367]

4. Lake County Trust Co. v. State Board of Tax Commissioners.[368]—Lake County Trust Company ("LCTC"), a real property owner with buildings constructed on the land, sought review of the ISBTC's final determination denying LCTC an economic obsolescence adjustment. LCTC leased the buildings to another company. Under the terms of the lease, LCTC was responsible for all property taxes assessed on the land and buildings.[369] LCTC presented evidence that other comparable properties did not provide for tax payment by the property owner and, therefore, the property in this case was less profitable as a result of the lease. Based on this difference, an expert testified, LCTC should be entitled to an economic obsolescence adjustment.[370]

The term "obsolescence" refers to the "'diminishing of a property's desirability and usefulness brought about by either functional inadequacies and overadequacies inherent in the property itself, or adverse economic factors external to the property.'"[371] ISBTC regulations provide for functional and economic loss of value.[372] ISBTC regulations list several permissible causes of economic obsolescence, including "[m]arket acceptability of the product or devices for which the property was constructed or is currently used."[373] LCTC argued that the market acceptability of the product, here the real estate under lease, justified an obsolescence depreciation adjustment.[374] The ISBTC countered that the facts of the case did not compare to any of the listed causes of economic obsolescence and that LCTC was not entitled to an adjustment. LCTC responded that the list of causes in the regulation was not an exhaustive list and, in any event, LCTC believed that the "market acceptability of the product" cause

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366. *See* IND. ADMIN. CODE tit. 50, r. 2.2-11-5.1(2)(B) (1996).

367. *Clark*, 694 N.E.2d at 1244 (citing IND. ADMIN. CODE tit. 50, r. 2.1-6-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-16-2(43) (1996))).

368. 694 N.E.2d 1253 (Ind. Tax Ct. 1998).

369. *See id.* at 1255.

370. *See id.*

371. *Id.* (quoting IND. ADMIN. CODE tit. 50 r. 2.1-6-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-16-2(43) (1996)).

372. *See id.* (citing IND. ADMIN. CODE tit. 50 r. 2.2-10-7(e)(2) (1996)).

373. *Id.* (quoting IND. ADMIN. CODE tit. 50 r. 2.1-5-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-7 (1996)).

374. *See id.*

fit the facts of this case.[375]

The court agreed with LCTC that the list of causes of economic obsolescence was not exhaustive, but also determined that the real estate of LCTC did not fit within any of the causes listed in the regulation.[376] The court found depreciation includes loss in value from all causes and thus, the list was not meant to be exhaustive.[377] The court then turned to whether the denial of an obsolescence adjustment was arbitrary and capricious. LCTC presented evidence that the market value of the property, as determined by what a willing buyer would pay, was depressed by as much as 48% because of the lease terms. However, because Indiana's property assessment tax system is not based on market value, the court found that the fact that a willing buyer would not pay as much because of the provisions in the lease was not dispositive.[378] Rather, to show economic obsolescence, LCTC was required to show that some factors external to the property caused the loss of value. In holding that LCTC failed to demonstrate economic obsolescence, the court pointed out that LCTC merely made a bad business decision that LCTC would like to now change.[379]

5. Loveless Construction Co. v. State Board of Tax Commissioners.[380]—Loveless Construction ("Loveless") leased office space in a building that Loveless owned. After the building was assessed, Loveless filed a petition for review with the CBOR and with the ISBTC. Still unsatisfied with the results of review, Loveless appealed to the tax court, claiming it was entitled to an obsolescence adjustment greater than 5%.[381] By statute, a taxpayer is entitled to an adjustment for a loss in value caused by obsolescence.[382]

Loveless first argued that the ISBTC's allowance of a 5% obsolescence adjustment was unsupported by the evidence.[383] The ISBTC countered that Loveless had not demonstrated that any additional obsolescence was warranted.[384] The court determined that even if Loveless had failed to demonstrate that additional obsolescence was appropriate, which the court did not believe was the case, it was still incumbent upon the ISBTC to support the grant of 5% as opposed to any other figure.[385] Having found that the ISBTC could not explain the facts relied upon in choosing the 5% figure, other than the subjective belief of the hearing officer, the court held that the ISBTC had not

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375. *See id.* at 1257.

376. *Id.* at 1257, 1258.

377. *Id.* at 1256 (citing IND. ADMIN. CODE tit. 50 r. 2.1-5-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-7 (1996)).

378. *Id.* at 1258.

379. *Id.* at 1259.

380. 695 N.E.2d 1045 (Ind. Tax Ct. 1998).

381. *See id.* at 1047.

382. *Id.* (citing IND. ADMIN. CODE tit. 50, r. 2.1-5-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-7(e) (1996))).

383. *See id.* at 1048.

384. *See id.*

385. *Id.*

supported the finding with substantial evidence.[386]

The court next examined whether Loveless had presented sufficient evidence to demonstrate that an obsolescence adjustment for an amount greater than 5% was justified. Loveless presented financial statements showing a decrease in income over a three-year period.[387] Further evidence presented tended to demonstrate that in order to keep the property fully occupied, Loveless had to change from net leases to gross leases.[388] Gross leases result in less gross income for the property owner because the lessor is required to pay expenses such as utilities and taxes.[389] A "cause of economic obsolescence is a decrease in the '[m]arket acceptability of the product or devices for which the property was constructed or is currently used.'"[390] The product in this case was the office space, and the court found that the change in lease terms from net leases to gross leases was evidence that the market considered the leases worth less than it had previously.[391] Consequently, the court held that Loveless had established a prima facie case of economic obsolescence and the ISBTC's failure to consider such in rendering its final assessment determination constituted an abuse of discretion.[392] The court remanded the case to the ISBTC for consideration of the amount of obsolescence to which Loveless was entitled, because neither party had supported its respective conclusion with substantial evidence.[393]

D. Indiana Property Taxes—Business Personal Property Tax

In *Monarch Steel Co. v. State Board of Tax Commissioners*,[394] Monarch Steel ("Monarch"), a steel service center located in Indiana, purchased steel plates, bars, and coils from companies inside and outside Indiana and sold such to customers both inside and outside Indiana.[395] In general, Monarch resold the bars and coils in the same form as received by Monarch. However, Monarch usually cut or changed the steel plates before reselling them.[396] Monarch argued that because of its operations, Monarch was entitled to an interstate commerce exemption for its business personal property for the tax years 1987 through 1995.[397] Indiana allows inventory to be exempt from property tax when located within Indiana if the inventory is merely within Indiana to be repackaged or is in

386. *Id.*

387. *See id.* at 1048-49.

388. *See id.*

389. *See id.* at 1048 n.2.

390. *Id.* at 1049 (quoting IND. ADMIN CODE tit. 50, r. 2.1-5-1 (1992) (recodified at IND. ADMIN. CODE tit. 50, r. 2.2-10-7 (1996))).

391. *Id.*

392. *Id.* at 1050.

393. *Id.*

394. 699 N.E.2d 809 (Ind. Tax Ct. 1998).

395. *See id.*

396. *See id.*

397. *See id.*

transit to a final destination (and kept within its original package).[398]

At the ISBTC hearing, Monarch provided the hearing officer with a box of receipts that Monarch alleged would prove that it was entitled to the exemption.[399] The ISBTC argued that simply giving the hearing officer a box of receipts, without more, did not present sufficient evidence that Monarch was entitled to the exemption.[400] The court noted that although the ISBTC is required to consider evidence submitted by a complaining taxpayer, the ISBTC is not required to make the case for the taxpayer.[401] Here, Monarch did not attempt to aid the hearing officer in understanding the invoices and provided no other evidence to the hearing officer as to why it was entitled to the exemption.[402] The hearing officer asked Monarch for information regarding the invoices, but Monarch failed to respond.[403] Based on these facts, the court held that Monarch failed to support its case with substantial evidence and upheld the ISBTC's final determination denying the exemption.[404]

E. Charitable Exemption From Indiana Taxes

1. Sangralea Boys Fund, Inc. v. State Board of Tax Commissioners.[405]—Sangralea Boys Fund ("Sangralea"), a not-for-profit company, provided assistance and education to disrupted children. In 1987, Sangralea leased part of its property to other not-for-profit organizations. For the years 1992 and 1993, both the CBOR and the ISBTC denied Sangralea's request for property exemptions.[406] At issue was the interpretation of Indiana's exemption statute, which provides that "[a]ll or part of a building is exempt from property taxation if it is owned, occupied, and used by a person for educational . . . or charitable purposes."[407]

The ISBTC maintained that to be entitled to the exemption, the unity of ownership, occupation, and use of the property must be by a single entity.[408] The current form of the statute is a recodification of a similar prior statute.[409] The 1975 recodification included an uncodified savings clause stating that the "'substantive operation and effect of any law repealed . . . shall continue without

398. *See id.* at 811 (citing IND. CODE §§ 6-1.1-10-29, -29.3, -30(a), (b), & (d) (1998)).

399. *See id.*

400. *See id.*

401. *Id.* at 812 (citing North Park Cinemas, Inc. v. State Bd. of Tax Comm'rs, 689 N.E.2d 765, 769 (Ind. Tax Ct. 1997)).

402. *See id.*

403. *See id.*

404. *Id.*

405. 686 N.E.2d 954 (Ind. Tax Ct. 1997).

406. *See id.* at 955.

407. *Id.* at 956 (quoting IND. CODE § 6-1.1-10-16(a) (1998)).

408. *See id.*

409. *See id.* at 957 (discussing IND. CODE ANN. § 6-1.1-10-16 (West 1989) (amended 1993, 1995)).

interruption if that law is reenacted, in the same or restated form, by this act.'"[410] The ISBTC claimed that this savings clause meant that the prior interpretation of unity of ownership by a single entity continued after promulgation of the new statute.

However, the court believed that the general assembly did not reenact the law in the same or restated form as contemplated by the savings clause, but instead eased the restrictions for obtaining a property exemption.[411] The court, in a footnote, also stated that even if the language of the statute had remained unchanged, the liberal construction that had been given to the Act would result in the same conclusion.[412] The court examined *State Board of Tax Commissioners v. Wright*,[413] wherein the court of appeals liberally construed the prior statute to allow a charitable organization flexibility in carrying out the charitable organization's mission and believed the same rationale applied to the facts of this case.[414]

The court supported its conclusion by examining other statutes passed with the same act. Section 6-1.1-10-37 of the Indiana Code provides that if property is leased from a tax-exempt entity to a taxable entity, it becomes taxable as if owned by the lessee.[415] The court held that Indiana Code section 6-1.1-10-16 "does not require a single entity to own, occupy, and use a piece of property before it can be exempted from taxation."[416] "Stated differently: a piece of property must be owned for charitable purposes; a piece of property must be occupied for charitable purposes; a piece of property must be used for charitable purposes."[417] This case potentially will have significant ramifications for tax-exempt organizations because tax-exempt organizations may now come together in an effort to more efficiently and effectively fulfill their missions without losing the tax benefits of their status.

2. Alte Salems Kirche, Inc. v. State Board of Tax Commissioners.[418]—Alte Salem Kirche ("Alte Salem"), a non-denominational church, owned a church building, a barn, and a mobile home, but not the land upon which these structures were located. The land was owned by Burgdorf, a director of the church.[419] According to Burgdorf, the mobile home was rented out to different persons for the purposes of having someone on the property to prevent vandalism and having a way to obtain insurance.[420] The barn was used to store equipment and picnic tables. Alte Salem was organized for the purpose of providing a place where

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410. *Id.* (quoting Act of Mar. 18, 1975, No. 45, § 5, 1975 Ind. Acts 247, 466).
411. *Id.*
412. *Id.* at 957 n.5.
413. 215 N.E.2d 57 (Ind. App. 1966).
414. *Sangralea*, 686 N.E.2d at 957.
415. *See id.* at 958 (citing IND. CODE § 6-1.1-10-37 (1998)).
416. *Id.* at 959.
417. *Id.*
418. 694 N.E.2d 810 (Ind. Tax Ct. 1998).
419. *See id.*
420. *See id.*

"people could attend to their spiritual needs."[421] Though the purpose of the church building was to provide a place where people could tend to their spiritual needs, the church building was often used by other churches and even other organizations not related to religion (e.g., Girl Scouts).[422] In this case, Alte Salem argued that it was entitled to an exemption for the improvements on the land and certain personal property, including the mobile home, for 1990.[423]

By statute, "'[a]ll or part of a building is exempt from property taxation if it is owned, occupied, and used by a person for educational, literary, scientific, religious, or charitable purposes.'"[424] Thus, if the improvements and personal property were used for religious or charitable purposes, Alte Salem would be entitled to an exemption. Alte Salem contended that it did use the improvements and personal property in furtherance of such goals. On the other hand, the ISBTC found that Alte Salem presented no evidence supporting the claim for exemption in light of the fact that in 1990 the property had primarily been used for non-religious activities such as picnics and reunions.[425] However, the court found sufficient uncontroverted evidence to conclude that the property likely was used for religious purposes.[426] According to the ISBTC, the court could only look at activities taking place in 1990 to determine whether Alte Salem engaged in religious activities. However, the court, citing *Governours Square Apartments v. State Board of Tax Commissioners*,[427] found that evidence of events occurring in other tax years, if relevant, is probative and should be considered by the ISBTC.[428] In cases such as this, the issue of primary concern is the purpose for which the property is being used and events outside the tax year in issue may be helpful in the determining this purpose.[429] Additionally, the fact that the church building may have been used for activities other than religion does not lead to the conclusion that exempt purposes were not furthered.[430] The court held that the ISBTC failed to consider all relevant evidence and remanded the issue to the ISBTC so it could consider evidence of activities conducted in years other than 1990.[431]

Alte Salem also argued that the barn and mobile home should be exempt from tax.[432] The ISBTC did not address this issue in its final determination.[433] The ISBTC, believing that Alte Salem did not use the property for exempt

421. *Id.* at 813.
422. *See id.*
423. *See id.* at 812.
424. *Id.* (quoting IND. CODE § 6-1.1-10-16(a) (1998)).
425. *See id.* at 814.
426. *Id.*
427. 528 N.E.2d 864, 866 (Ind. Tax Ct. 1988) (citations omitted).
428. *Alte Salems*, 694 N.E.2d at 814.
429. *See id.*
430. *See id.*
431. *Id.* at 816.
432. *See id.* at 815.
433. *See id.*

purposes, merely assumed that the barn and mobile home would not be exempt if the church building was not exempt.[434] Property that is "'incidental and necessary for the effective welfare of [an] exempt religious institution' is exempt from property taxation."[435] The court, finding that the ISBTC did not consider Alte Salem's argument, also remanded to the ISBTC the issue of whether the barn and mobile home were "incidental and necessary" to an exempt purpose.[436]

3. Trinity Episcopal Church v. State Board of Tax Commissioners.[437]— Shortly after Trinity Episcopal Church ("Trinity") purchased a building and a parking lot, Midtown Community Mental Health Center ("Midtown") became interested in the property for use as a mental health center.[438] Midtown, however, did not have the necessary capital to renovate the building.[439] Consequently, Trinity and Midtown entered into an agreement whereby Trinity would finance the renovations and Midtown would repay the costs over a long-term lease. On July 12, 1995, shortly after the renovations were completed, Midtown leased the property from Trinity.[440] The ISBTC granted Trinity an exemption for the parking lot because it was owned, occupied, and used for exempt purposes. However, because the building was vacant on March 1, 1995, the date of the assessment, the exemption for the building was denied.[441] Trinity appealed, contending that it was entitled to an exemption.

"'All or part of a building is exempt from property taxation if it is owned, occupied, and used by a person for educational, scientific, religious, or charitable purposes.'"[442] The court, relying on the similar case of *Foursquare Tabernacle Church of God in Christ v. State Board of Tax Commissioners*,[443] held that Trinity was entitled to an exemption.[444] In *Foursquare*, the court held that "property acquired for future use in furtherance of exempt purposes may qualify for a property tax exemption under section 6-1.1-10-16."[445] Therefore, it was only necessary that Trinity establish that it had the intent to use the building in furtherance of an exempt purpose as of the date of the assessment. On the other hand, the ISBTC, citing *Stark v. Kreyling*,[446] argued that only those facts existing on March 1, 1995 could be taken into account in determining whether Trinity

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434. *See id.*

435. *Id.* (quoting LeSea Broad. Corp. v. State Bd. of Tax Comm'rs, 525 N.E.2d 637, 639 (Ind. Tax Ct. 1988) (other citations omitted)).

436. *Id.* at 816.

437. 694 N.E.2d 816 (Ind. Tax Ct. 1998).

438. *See id.* at 817.

439. *See id.*

440. *See id.*

441. *See id.*

442. *Id.* at 818 (quoting IND. CODE ANN. § 6-1.1-10-16(a) (West Supp. 1997) (amended at IND. CODE § 6-1.1-10-16(a) (1998)).

443. 550 N.E.2d 850 (Ind. Tax Ct. 1990).

444. *Trinity*, 694 N.E.2d at 818.

445. *Id.* (citing *Foursquare*, 550 N.E.2d at 854).

446. 188 N.E. 680, 681 (Ind. 1934).

was exempt from property tax.[447] Because the renovations were not complete on March 1, 1998, the ISBTC argued that Trinity was not entitled to an exemption.[448] According to the court, Trinity had the requisite intent to use the property for exempt purposes in light of the fact that it had incurred significant renovation expenses and already had an agreement with Midtown.[449] Therefore, the court held that it was an abuse of discretion to deny Trinity the exemption.[450]

F. Indiana Procedures For Tax Administration—Indiana State Board of Tax Commissioners

In *Kent Co. v. State Board of Tax Commissioners*,[451] Kent owned real property that was assessed during the 1989 general assessment.[452] Kent petitioned the CBOR to review the assessment, filing a Form 130.[453] The CBOR issued a final assessment with which Kent disagreed. Kent then filed a Form 131 Petition for Review with the ISBTC.[454] The ISBTC issued a final determination, lowering the assessment and Kent did not appeal the determination.[455] During the assessment review process, Kent paid property taxes based on the 1988 assessed value of its property.[456] After the ISBTC issued its final determination, the county treasurer sent Kent a revised tax bill that was higher than the initial tax bill, because it was based on the 1988 assessed value.[457] Kent then filed a petition for review with the CBOR and the CBOR denied the petition, stating that the petition was not timely filed.[458] Kent sought review with the ISBTC, which took no action for over twelve months.[459] The issue before the court was whether the court had jurisdiction to determine a challenge to the assessed property value.

Kent argued that the initial tax bills reflected the ISBTC's assessment for each year as opposed to the 1988 assessment, and that as a result, the increase in tax liability was a sua sponte assessment, completed without notice and an opportunity for a hearing.[460] The court addressed two claims made by Kent: (1)

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447. *See Trinity*, 698 N.E.2d at 819.
448. *See id.*
449. *Id.* at 818.
450. *Id.* at 819.
451. 685 N.E.2d 1156 (Ind. Tax Ct. 1997).
452. *See id.*
453. *See id.* at 1156 n.2 (citing IND. CODE § 6-1.1-15-1 (1998) (amended eff. Jan. 1, 1999); IND. ADMIN. CODE tit. 50, r. 4.2-3-3 (1996)).
454. *See id.* at 1156 n.3 (citing IND. CODE § 6-1.1-15-3 (1998) (amended eff. Jan. 1, 1999); IND. ADMIN. CODE tit. 50, r. 4.2-3-3 (1996)).
455. *See id.* at 1156.
456. *See id.* at 1156-57 (citing IND. CODE § 6-1.1-15-10(a)(2) (1998)).
457. *See id.* at 1157.
458. *See id.*
459. *See id.*
460. *See id. See also* IND. CODE §§ 6-1.1-9-4, -14-11 (1998) (requiring notice and an opportunity for a hearing).

whether the 1989 assessment was incorrect; and (2) whether the notice given as to the increase in assessment was improper.[461] As to the first of Kent's claims, the court held that it had "no jurisdiction to entertain any dispute about the validity of the 1989 assessment."[462]

> What Kent really is seeking to do here is collaterally attack the 1989 assessment as it applied to the tax years in issue. The time to assert error in the 1989 assessment as it applied to the tax years in issue in this Court was December 21, 1992 (forty-five days after the final determination by the State Board). After the forty-five days expired, this Court had no jurisdiction to hear Kent's appeal of the 1989 assessment as applied to the tax years at issue. (Of course, Kent's failure to appeal the State Board's final determination did not foreclose Kent's ability to challenge the 1989 assessment as it applied to other years.) Kent cannot confer that jurisdiction by reinitiating the Form 130/131 process and then filing an original tax appeal. Therefore, this Court has no jurisdiction to evaluate Kent's assertion that the 1989 assessment was erroneous as applied to the tax years in issue.[463]

As to the second of Kent's claims, the court held that the revised tax bill was valid.[464] When a challenge is made, a taxpayer must make property tax payments based on the immediately preceding year.[465] However, any increased amount in dispute need not be paid until after the petition for review is finally adjudicated.[466] As the review process progressed, taxes accrued for the years 1990 through 1992 and Kent paid the property taxes for those years based on the 1988 assessment. Kent claimed that the initial tax bills represented an assessment and that the revised tax bill, sent only after final adjudication of the review process, constituted a sua sponte increase in assessment.

The court pointed out that the initial tax bills were required by statute only as a provisional tax liability subject to change by the outcome of the 1989 assessment under review.[467] "Because the use of the 1988 value did not constitute an assessment, the subsequent revision of Kent's tax liability to reflect the [ISBTC's] final determination of the assessed value of Kent's property did not constitute a [sua sponte] increase in assessment."[468] Because the action was not a sua sponte increase in assessment, notice and an opportunity for a hearing were not required.[469] Therefore, the court dismissed Kent's tax appeal because the court lacked jurisdiction and entered summary judgment in favor of the

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461. *Kent*, 685 N.E.2d at 1157.
462. *Id.* at 1161.
463. *Id.* at 1158-59 (citation omitted).
464. *Id.* at 1161-62.
465. *See id.* at 1160 (citing IND. CODE § 6-1.1-15-10(a)(2) (1998)).
466. *See id.*
467. *Id.* at 1161.
468. *Id.*
469. *See id.*

ISBTC.[470]

G. Indiana Sales and Use Taxes

1. Rotation Products Corp. v. Department of State Revenue.[471]—Rotation Products Corporation ("RPC") repairs and remanufactures roller bearings.[472] After inspection of non-operational roller bearings, RPC determined whether the damaged roller bearings were to be scrapped, remanufactured, or merely cleaned and polished.[473] When RPC remanufactured the bearings, the inner and outer rings were ground down, and as a consequence, the thickness of the rings changed.[474] As a result of the change in thickness, a new rolling cage and rollers had to be fabricated so that the cage and rollers would fit between the new inner and outer rings.[475] The Indiana Department of State Revenue ("IDSR") and RPC disputed whether the equipment used and the materials consumed in remanufacturing the non-operational roller bearings were exempt from sales tax. The IDSR denied the exemption for the tax years 1990 through 1992 and RPC appealed.[476]

Indiana imposes a sales tax[477] on retail transactions in Indiana and a use tax[478] on tangible personal property used in Indiana. However, the general assembly has provided several exemptions from sales and use taxes, including "[t]ransactions involving manufacturing machinery, tools, and equipment . . . if the person acquiring that property acquires it for direct use in the direct production, manufacture, fabrication, assembly, extraction, mining, processing, refining, or finishing of other tangible personal property"[479] and "[t]ransactions involving tangible personal property . . . if the person acquiring that property acquires it for direct consumption as a material to be consumed in the direct production of other tangible personal property in the person's business of manufacturing, processing, refining, repairing."[480] The purpose behind exempting equipment and materials from the sales and use taxes is to encourage economic growth and limit multiple taxation.[481] The central issue in this case was whether the remanufacture of non-operational roller bearings constituted new tangible personal property within the meaning of the exemption statute.

The IDSR argued that RPC merely repaired the damaged bearings to a useful

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470. *Id.* at 1161-62.
471. 690 N.E.2d 795 (Ind. Tax Ct. 1998).
472. *See id.* at 797.
473. *See id.*
474. *See id.*
475. *See id.*
476. *See id.* at 796.
477. *See id.* at 797 (citing IND. CODE § 6-2.5-2-1 (1998)).
478. *See id.* (citing IND. CODE § 6-2.5-3-2 (1998)).
479. *See id.* at 798 (citing IND. CODE § 6-2.5-5-3(b) (1998)).
480. *Id.* (citing IND. CODE § 6-2.5-5-5.1(b) (1998)).
481. *See id.*

condition; thus, a service activity was performed that is subject to sales tax.[482] The IDSR claimed that any form of repair could not be considered "production" within the meaning of the exemption statute because such repair was a service activity.[483] RPC countered that it took raw materials (unuseable roller bearings) and transformed them into a new, useable product.[484] The tax court determined that a repair activity could constitute production: "[A]t some point, the repair activity is so extensive in nature and so transforms the object such that it cannot be characterized as a mere service. Rather, the repair activity produces a new product and therefore constitutes exempt activity."[485] The court stated that to constitute "production," the activity in question must generally entail a substantial amount of work that caused the end product to be "'substantially different from the component materials used.'"[486]

To determine whether an activity constitutes "production" within the meaning of the exemption statute, the court focused on the following factors: (1) "the substantiality and complexity of the work done on the existing article and the physical changes to the existing article, including the addition of new parts;"[487] (2) "a comparison of the article's value before and after the work;"[488] (3) "how favorably the performance of the remanufactured article compared with the performance of newly manufactured articles of its kind;"[489] and, (4) "whether the work performed was contemplated as a normal part of the life cycle of the existing article."[490] The court then evaluated the remanufacturing process of the roller bearings to determine whether RPC produced new tangible personal property during such process.

The court determined that RPC performed substantial and complex work such that the bearings were physically changed during the process due to the grinding and polishing of the old rings, along with fabrication of a new rolling cage and elements.[491] Second, the court found that the value of the remanufactured roller bearing was significantly increased over the value of the non-operational bearing.[492] Third, the court found that the remanufactured bearing was at least as good or better than a newly manufactured roller bearing, as evidenced by RPC's guarantee that the load capacity would be greater than the load capacity was when the roller bearings were new.[493] Finally, the court found

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482. *See id.* at 800.

483. *See id.*

484. *See id.*

485. *Id.* at 801.

486. *Id.* at 802 (quoting Mechanics Laundry & Supply, Inc. v. Department of State Revenue, 650 N.E.2d 1223,1229 (Ind. Tax Ct. 1994)).

487. *Id.* at 802-03.

488. *Id.* at 803.

489. *Id.*

490. *Id.*

491. *Id.*

492. *Id.*

493. *Id.*

that the remanufacturing was not contemplated as a normal part of the life-cycle of the roller bearing, particularly because of the fact that when a customer took the non-operational bearing to RPC, it was not known at that time whether the bearings could even be salvaged.[494]

Upon evaluation of the four factors, the court held that RPC produced "other tangible personal property" as contemplated by the exemption statute.[495] The court further held that even if RPC only cleaned and polished the inner and outer rings (as opposed to additionally fabricating a new roller cage), RPC would still be entitled to the exemption for cleaning and polishing because those processes are integral parts of the operation of producing other tangible personal property.[496] The court also found that granting an exemption in this case would further serve the legislative purposes of encouraging economic growth and avoiding multiple taxation or tax pyramiding.[497]

This case may give a greater number of companies the ability to claim an industrial tax exemption, providing the companies satisfy the above-stated four factors. Notably, new tangible personal property must be produced that is sufficiently different from the beginning product. Additionally, to be entitled to an exemption for repairs, the process must not be one contemplated during the ordinary life cycle of the original product.

2. Indianapolis Fruit Co. v. Department of State Revenue.[498]—Indianapolis Fruit, a supplier of fruits and vegetables, received bananas and tomatoes in an unmarketable form.[499] The bananas arrived green and unripe. In order to market the bananas, Indianapolis Fruit exposed the bananas to ethylene gas. Additionally, Indianapolis Fruit inspected the pulp for temperature, firmness, temperature damage and overall quality.[500] Indianapolis Fruit controlled the environment of the bananas throughout the ripening process and but for this process, the bananas would have turned from green to black, instead of from green to yellow.[501] The ripening process also converted the starch within the banana into sugar.[502] During the ripening process, which lasted between four to eight days, the bananas were inspected several times a day.[503]

The tomato ripening process was similar to the banana ripening process. However, Indianapolis Fruit usually did not expose the tomatoes to ethylene gas because many of its suppliers performed this activity.[504] The tomatoes were

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494. *Id.*

495. *Id.* at 804.

496. *Id.* (citing Department of State Revenue v. Cave Stone, Inc. 457 N.E.2d 520, 524 (Ind. 1983).

497. *Id.* at 805.

498. 691 N.E.2d 1379 (Ind. Tax Ct. 1998).

499. *See id.* at 1381.

500. *See id.*

501. *See id.*

502. *See id.*

503. *See id.* at 1382.

504. *See id.*

placed in a controlled environment and the temperature, humidity, and air circulation were monitored.[505] Once the tomatoes ripened, they were either shipped in bulk or packaged by Indianapolis Fruit for later shipment.[506]

In addition to the banana and tomato ripening processes, Indianapolis Fruit operated a garden cut facility that supplied fresh fruits and vegetables to grocery stores and restaurants.[507] Employees in direct contact with the food were required to wear hair restraints, lab coats, vinyl gloves, and neoprene aprons and sleeves.[508] Those employees who were not in direct contact with food were only required to wear hair restraints.[509]

Indiana imposes a sales tax[510] on retail transactions and a use tax[511] on tangible personal property used within Indiana. Indiana also provides exemption from such taxes. The IDSR denied Indianapolis Fruit exemptions for the materials and machinery used in the banana and tomato processes and denied an exemption for the protective clothing worn in the garden cut facility. Indianapolis Fruit appealed. The company contended that the tangible personal property used in the banana and tomato ripening processes were exempt from sales and use taxes.[512] Indianapolis Fruit also claimed that the machinery, tools, and equipment used to produce "other tangible personal property" were exempt from taxation.[513]

Before materials or machinery can be exempt from sales and use taxation, it must be shown that the taxpayer engaged in "production" within the meaning of the statute.[514] Once it is established that an activity constitutes production, the taxpayer must demonstrate that the items claimed to be exempt are "integral and essential to that production."[515] For a product to satisfy this element, the product must be placed in a "'form, composition, or character substantially different from that in which [they] w[ere] acquired.'"[516]

Indianapolis Fruit contended that it was engaged in activities constituting production. The court first examined whether the banana ripening process constituted production of "other tangible personal property." Indianapolis Fruit argued that it changed unripe and non-marketable bananas into ripened marketable bananas, and therefore, it engaged in production.[517] The IDSR

505. *See id.*

506. *See id.*

507. *See id.*

508. *See id.*

509. *See id.*

510. *See id.* at 1383 (citing IND. CODE § 6-2.5-2-1 (1998)).

511. *See id.* (citing IND. CODE § 6-2.5-3-2 (1998)).

512. *See id.* (citing IND. CODE §§ 6-2.5-5-1, -2 (1998)).

513. *See id.* (citing IND. CODE § 6-2.5-5-3(b) (1998)).

514. *See id.* at 1383.

515. *Id.* at 1384 (citing Department of State Revenue v. Cave Stone, 457 N.E.2d 520, 524 (Ind. 1983)).

516. *See id.* at 1385 (quoting IND. ADMIN. CODE tit. 45, r. 2.2-5-10(k) (1996)).

517. *See id.*

countered that Indianapolis Fruit merely controlled the banana's ripeness.[518] However, the court found that because the bananas underwent a substantial change, the process constituted production.[519] The court focused on the fact that without action by Indianapolis Fruit, the bananas would not have ripened, and because there was production, the court held that Indianapolis Fruit was entitled to an exemption for all items "integral and essential" to the ripening process.[520] The court described the "integral and essential" items as all items from the beginning of the process (when the bananas were placed in the ripening booths) to the end of the process (when the bananas were packaged for shipment).[521]

The court next addressed whether the tomato ripening process constituted production of "other tangible personal property" as contemplated by the exemption statute. The court held that the tomato ripening process did not constitute production.[522] Unlike the banana ripening process, Indianapolis Fruit did not trigger the ripening of the tomatoes. Rather, Indianapolis Fruit merely awaited the ripening of the tomatoes before distribution.[523] Though Indianapolis Fruit did control the environment and increase the marketability of the tomatoes, it did not actively induce the ripening.[524] Indianapolis Fruit was not entitled to receive an exemption merely because the tomatoes ripened while in their possession.[525] To be considered production, Indianapolis Fruit would have to do something more than passively await the tomatoes to ripen.[526] The court also denied an exemption for the packaging of the tomatoes for resale.[527] Even though packaging may be an integral part of a production process, this did not mean that the packaging in and of itself constituted production because "the packaging [did] not change[] the 'form, composition, or character' of the tomatoes."[528] As to an exemption for the protective clothing worn by employees in the garden cut facility, the court held that Indianapolis Fruit was entitled to the exemption because the clothing was necessary to prevent contamination, as provided for in an IDSR regulation.[529]

3. White River Environmental Partnership v. Department of State Revenue.[530]—White River Environmental Partnership ("WREP") treats wastewater so that it can be discharged into the White River.[531] The wastewater

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518. *See id.* at 1384-85.
519. *Id.* at 1385.
520. *Id.*
521. *Id.*
522. *Id.*
523. *See id.*
524. *See id.*
525. *See id.*
526. *See id.*
527. *Id.* at 1386.
528. *Id.* (quoting IND. ADMIN. CODE tit. 45, r. 2.2-5-8(k) (1996)).
529. *Id.*
530. 694 N.E.2d 1248 (Ind. Tax Ct. 1998).
531. *See id.* at 1249.

treatment process is very extensive. As wastewater enters, WREP adds chemicals to control odors and coagulate the solids, and the water then goes through a process that removes plant matter and egg shells.[532] Next, the larger solids are removed, followed by aeration that allows bacteria to attack any remaining solids. Finally, the wastewater is disinfected and ultimately discharged into the White River.[533]

Indiana imposes a sales tax,[534] with certain exemptions, on retail transactions and a use tax[535] on tangible personal property stored, used, or consumed within Indiana. WREP argued that it was entitled to the consumption exemption and the environmental quality exemption.[536] The consumption exemption provides, in part, that transactions are exempt from sales tax "'if the person acquiring the property acquires it for direct consumption as a material to be consumed in the direct production of other tangible personal property.'"[537] The environmental quality exemption provides that sales are exempt from tax if:

> "(1) the property constitutes, is incorporated into, or is consumed in the operation of a device, facility, or structure predominantly used and acquired for the purpose of complying with any state . . . environmental quality statute[] . . .; and (2) the person acquiring the property is engaged in the business of manufacturing, processing, refining, mining, or agriculture."[538]

Both provisions require that WREP engage in production to receive the exemption.

WREP argued that it was engaged in "production" because it makes clean water that can be used in irrigation, ash that can be used in making brick, and sludge that can be used as a fertilizer.[539] Additionally, WREP substantially changes the wastewater it receives.[540] The court agreed that WREP changed the wastewater to a "'a form, composition, or character substantially [sic] different from that in which it was acquired.'"[541] However, this change in the form or composition of wastewater did not establish the fact that WREP engaged in production as contemplated by the exemption provision.[542] In this case, the products of the wastewater treatment facility were not sold; therefore, there was no need for an exemption to prevent tax pyramiding, a major purpose of the

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532. *See id.*
533. *See id.*
534. *See id.* at 1251 (citing IND. CODE § 6-2.5-2-1 (1998)).
535. *See id.* (citing IND. CODE § 6-2.5-3-2 (1998)).
536. *See id.* (citing IND. CODE § 6-2.5-5-30 (1998)).
537. *Id.* (quoting IND. CODE § 6-2.5-5-5.1 (1998)).
538. *Id.* (quoting IND. CODE § 6-2.5-5-30 (1998)).
539. *See id.* at 1251.
540. *See id.*
541. *Id.* (quoting IND. ADMIN. CODE tit. 45, r. 2.2-5-10(k) (1996)).
542. *See id.*

exemption provision.[543] Despite the fact that wastewater treatment is an important public interest that would be promoted by granting an exemption, the court held that the statute was not meant to grant an exemption in this case because WREP had not engaged in "production of other tangible personal property" as contemplated by the exemption provision.[544] The court noted that it was up to the general assembly, not the courts, to address any inadequacies of the exemption statute.

4. Hyatt Corp. v. Department of State Revenue.[545]—Hyatt purchased unprepared food for the purpose of preparing and serving complimentary meals to certain members and employees.[546] The IDSR instituted an audit and discovered an unpaid tax liability.[547] During the proceedings, Hyatt contended that it was entitled to offset the tax liability with use tax erroneously paid on its food purchases.[548] However, Hyatt paid the assessment and then filed a claim for a refund for the amount of overpayment of use tax.[549] The IDSR denied the refund claim and Hyatt appealed.[550]

Indiana imposes a sales tax[551] on retail transactions and a use tax[552] on tangible personal property stored, used, or consumed within Indiana. Indiana also provides for exemption from certain sales and use taxes. Hyatt claimed that its purchases of food were exempt under an exemption statute that provides: "Sales of food for human consumption are exempt from the state gross retail tax."[553] The exemption provision also defined "food for human consumption" and listed several types of food that were not to be considered food for human consumption.[554] Hyatt argued that it was entitled to an exemption because its activities were not listed as an exclusion from the exemption.

The IDSR made several arguments contending that Hyatt was not entitled to an exemption. First, the IDSR argued that Hyatt could not claim an exemption because it did not sell the prepared food and consequently had not collected or paid sales tax on the food.[555] According to the IDSR, this meant that the food purchases were taxable. Second, the IDSR attempted to show that Hyatt did not fall within the class of persons that the general assembly intended to benefit.[556] However, the court viewed the IDSR's arguments as attempts to add restrictions

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543. *See id.* at 1251-52.
544. *See id.* at 1252.
545. 695 N.E.2d 1051 (Ind. Tax Ct. 1998).
546. *See id.* at 1052.
547. *See id.*
548. *See id.*
549. *See id.*
550. *See id.*
551. *See id.* at 1053 (citing IND. CODE § 6-2.5-2-1 (1998)).
552. *See id.* (citing IND. CODE § 6-2.5-3-2(a) (1998)).
553. *Id.* at 1054 (quoting IND. CODE § 6-2.5-5-20 (1998)).
554. *See id.*
555. *See id.* at 1055.
556. *See id.* at 1054.

to the availability of the exemption.[557] The plain language of the statute had no such restrictions and the court refused to read such restrictions into the exemption provisions.[558] The court held that Hyatt was entitled to a tax exemption for the purchase of food and stated: "But that escape is with the legislature's blessing; consequently, it is not for this court to prevent the escape simply because it deems a taxpayer unworthy of receiving an exemption. The legislature decides which taxpayer deserves to escape taxation."[559]

H. Indiana Motor Carrier Fuel Taxes

In *Bulkmatic Transport Co. v. Department of State Revenue*, Bulkmatic Transport ("Bulkmatic") is a trucking company that serves customers both inside and outside Indiana.[560] Power take off ("PTO") equipment, attached to the delivery truck, was used to unload cargo. The PTO equipment was powered by fuel from the same tank as the engine and the average amount of fuel consumed during an unloading was seven gallons.[561] Trucking companies are taxed on the fuel consumed while using Indiana roads.[562] The companies are taxed on the percentage of fuel used in Indiana by calculating the amount of miles traveled on Indiana highways compared to the total amount of fuel consumed on all nationwide highways.[563] The fuel used by PTO equipment, assuming the equipment is powered from the same tank as the engine, is also used in determining the amount of tax owed. Indiana has an exemption statute for the use of fuel during offloading with PTO equipment to ameliorate the additional tax liability.[564] However, the general assembly limited the exemption to carriers who use PTO equipment "'in Indiana.'"[565] The exemption amount is not determined by the amount of fuel consumed during unloading with PTO equipment, but rather a motor carrier is reimbursed 15% of the total amount of tax paid for fuel consumption when PTO equipment is used "in Indiana."

Bulkmatic argued that the exemption statute was unconstitutional as violative of the Commerce Clause of the U.S. Constitution. The Commerce Clause grants Congress the "'Power . . . [t]o regulate Commerce . . . among the several States.'"[566] The court stated that the tax would be upheld if "'the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the

557. *See id.* at 1056.
558. *Id.*
559. *Id.* at 1055-56.
560. *See id.* at 1372.
561. *See id.* at 1372-73.
562. *See id.* at 1372 (citing IND. CODE §§ 6-6-4.1-4, -4.5 (1998)).
563. *See id.* at 1373.
564. *See id.*
565. *Id.* (quoting IND. CODE § 6-6-4.1-4(d) (1998)).
566. *Id.* at 1374 (quoting U.S. CONST. art. I, § 8, cl. 3).

services provided by the State.'"[567] Bulkmatic argued that requiring the PTO equipment to be used "in Indiana" in order to qualify for the exemption discriminates against interstate commerce.[568] The IDSR countered that this system was not discriminatory because it treats in-state and out-of-state companies equally.[569] The court noted that the U.S. Supreme Court has held that it is unconstitutional to "'tax . . . a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the state.'"[570]

The court discussed three cases and how they affected the outcome of this case. In *Camps Newfound/Owatonna v. Town of Harrison*,[571] the U.S. Supreme Court invalidated a property tax as violating the Commerce Clause because charitable organizations that catered to non-residents were given a reduced tax exemption as compared with charitable organizations catering to residents. The Supreme Court reasoned that the exemption statute encouraged organizations to limit the out-of-state participants.[572] Similar to *Camps Newfound*, the *Bulkmatic* court stated that limiting the exemption to offloads "in Indiana" encouraged carriers to limit deliveries to customers within Indiana to take advantage of the tax exemption.[573]

In *Boston Stock Exchange v. State Tax Commission*,[574] New York imposed a tax on sales of securities. However, New York taxed out-of-state transactions more heavily than in-state transactions.[575] The Supreme Court ruled that the exemption for in-state status was discriminatory.[576] The tax court analogized *Boston Stock Exchange* to *Bulkmatic*, finding that "[l]ike the New York exemption scheme, the 'in Indiana' exemption does not result in 'substantially evenhanded treatment' of motor carriers."[577] Additionally, the court discussed *Westinghouse Electric Corp. v. Tully*,[578] wherein the Supreme Court again struck down a New York statute because the statute placed a "'discriminatory burden on commerce to sister States.'"[579] Like *Westinghouse*, the statute in *Bulkmatic* impermissibly discriminated against out-of-state interests.[580]

According to the IDSR, the exemption did not discriminate against interstate commerce. The IDSR claimed that because it did not differentiate between in-state and out-of-state companies, the statute did not violate interstate

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567. *Id.* at 1376 (quoting Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977)).
568. *See id.* at 1375.
569. *See id.*
570. *Id.* at 1376 (quoting Fulton Corp. v. Faulkner, 516 U.S. 325, 331 (1996)).
571. 520 U.S. 564 (1997).
572. *Id.* at 579.
573. *Bulkmatic*, 691 N.E.2d at 1376-77.
574. 429 U.S. 318 (1977).
575. *See Boston Stock Exch.*, 429 U.S. at 319.
576. *Id.*
577. *Bulkmatic*, 691 N.E.2d at 1378.
578. 466 U.S. 388 (1984).
579. *Id.* at 406 (citing *Boston Stock Exch.*, 429 U.S. at 331).
580. *Bulkmatic*, 691 N.E.2d at 1378.

commerce.[581] However, the court found that because the exemption statute encouraged deliveries into Indiana and taxed transactions more heavily once the deliveries crossed state lines, the statute violated the Commerce Clause.[582]

The IDSR also contended that the statute provided a generous exemption from taxes and was merely a means of assuring calculation of the amount of such exemption.[583] However, the court stated that a generous intent or purpose does not insulate a statute from the mandates of the Commerce Clause.[584] Finally, the IDSR claimed that this was not a case of discrimination, but rather a lack of exactness. According to the IDSR, even though two companies may be taxed differently for using the same amount of Indiana's highway, it was not required to formulate precisely the amount of fuel consumed and tax owed.[585] However, the court stated that if a statute is found to discriminate against interstate commerce, then the statute must be struck down as violating the Commerce Clause.[586] The court held that the "'in Indiana' limitation on Indiana's motor carrier fuel tax exemption discriminated against interstate commerce and . . . is not allowed under the Commerce Clause."[587]

I. Indiana Excise Taxes

In *Horrall v. Indiana Department of State Revenue*,[588] Horrall appealed a final determination of the IDSR claiming that the IDSR erroneously assessed a Controlled Substance Excise Tax ("CSET") and that Horrall was entitled to a refund of the tax that was paid by levy.[589] Horrall made the following challenges to the legality of the IDSR's assessment: (1) Horrall was an ultimate user of the marijuana and not liable for the tax; (2) other persons are liable for the tax; (3) the date of the assessment, May 20, 1997, renders the assessment fatally defective because Horrall was incarcerated on that date and did not possess the marijuana on that date; and (4) the tax statute was void for vagueness.[590]

A CSET is a tax imposed on those who possess a controlled substance, unless such person has a legal justification for possessing the controlled substance.[591] Horrall argued that because he was an ultimate user, he had a legal justification.[592] However, an ultimate user is defined by statute as "a person who

581. *See id.*
582. *Id.*
583. *See id.* at 1379.
584. *Id.*
585. *See id.*
586. *Id.*
587. *Id.*
588. 687 N.E.2d 1219 (Ind. Tax Ct. 1997).
589. *Id.* at 1220.
590. *See id.*
591. *See id.* at 1220-21 (citing IND. CODE § 6-7-3-5 (1998)).
592. *See id.* at 1221.

lawfully possess a controlled substance."[593] Consequently, Horrall's challenge to the assessment on this basis failed.

Horrall next argued that others possessed or manufactured the controlled substance on the same day that Horrall was assessed the CSET and therefore, he cannot be liable for the tax.[594] However, the court pointed out that even though others may be obligated to pay a tax, it would not relieve Horrall from his liability.[595] Similarly, even if Horrall did not manufacture the marijuana, it is possession of such substance that triggers a tax liability.[596]

Horrall also argued that the assessment was defective because the notice of assessment listed a day in which he was incarcerated, and therefore, he could not have possessed the marijuana on that date.[597] The IDSR countered that this technical error did not prejudice Horrall in any way. The court stated that the purpose of the notice of proposed assessment is to inform the taxpayer that he may owe taxes, provide protest information, and begin the running of the sixty-day period in which to file a written protest.[598] Pointing out that the notice of proposed assessment serves an important function, the court determined that because Horrall was not prejudiced (he did not fail to file a written protest nor was the preparation of his case impaired), his claim must fail.[599]

Finally, Horrall argued that the statute making possession of marijuana criminal was void for vagueness.[600] Statutes are required to be sufficiently definite so that an individual will know what conduct is legal or illegal, and the court held that the statute in question was "exceedingly clear."[601] Ultimately, the court found that Horrall was liable for the tax because he unlawfully possessed a controlled substance.[602]

An important aspect of this case is the fact that the court held, absent actual prejudice to a taxpayer, that no relief will be afforded when there is merely a slight factual error in a notice of proposed assessment. What the court will consider a "slight" factual error or what types of error actually prejudice a taxpayer were not determined in this case; these may become hurdles for future petitioning taxpayers.

J. Indiana Inheritance Taxes

In *Department of State Revenue v. Estate of Phelps*,[603] Phelps, the decedent,

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593. *Id.* (citing IND. CODE § 35-48-1-27 (1998)).
594. *See id.*
595. *Id.*
596. *See id.*
597. *See id.*
598. *Id.*
599. *Id.* at 1221-22.
600. *See id.* at 1222.
601. *Id.*
602. *Id.*
603. 697 N.E.2d 506 (Ind. Tax Ct. 1998).

died testate on December 3, 1994.[604] By the terms of the decedent's last will and testament, the decedent's spouse received all tangible personal property and her interest in the marital home. The remainder passed by a residuary clause into a revocable trust.[605] Under the trust, the spouse received $200,000. The other assets were divided into two trusts, one marital and the other non-marital.[606] The marital trust granted the surviving spouse an income interest for life, remainder to the children.[607] The corpus of the trust could be invaded for the surviving spouse's care, comfort, or maintenance. On July 17, 1995, the estate filed an Indiana inheritance tax return, attaching the decedent's will and the trust agreement.[608] On November 29, 1995, within the twelve-month period for which inheritance returns are due, the estate filed a second Indiana inheritance tax return, this time attaching a qualified terminable interest property ("QTIP") election.[609]

Indiana imposes an inheritance tax on certain transfers at death and the amount is based on the fair market value of the property.[610] Property passed to a surviving spouse is exempt from Indiana inheritance tax.[611] However, the remainder interest (the value of the remainder to the children) is subject to Indiana inheritance taxation unless a QTIP election is filed within the proper time and in the proper form.[612] The IDSR regulations provide the form with which an election must substantially comply.[613]

In this case, the estate did not file a QTIP election on July 17, the date the estate filed its original inheritance tax return. Therefore, the court held that the estate did not make a proper QTIP election in filing the first inheritance return.[614] Although the second inheritance return did have a QTIP election attached to the return, by regulation a QTIP election "'must be in writing, signed by a person authorized to make the election, and attached to the original Indiana inheritance tax return at the time it is filed.'"[615] Any mistake in making a QTIP election is treated as an irrevocable election not to treat the transaction as a QTIP transfer.[616]

The IDSR argued that because the QTIP election was not "attached to the original inheritance tax return," the election was invalid. The estate, however, claimed that because the phrase, "attached to the original inheritance tax return," was not defined by statute or under the regulations, the court should apply the

604. *See id.* at 508.
605. *See id.*
606. *See id.*
607. *See id.*
608. *See id.*
609. *See id.* at 508-09.
610. *See id.* at 509 (citing IND. CODE §§ 6-4.1-2-1, 6-4.1-5-1.5 (1998)).
611. *See id.* (citing IND. CODE § 6-4.1-3-7(a) (1998)).
612. *See id.* (citing IND. CODE ANN. § 6-4.1-3-7(c) (1998)).
613. *See id.* at 510 (citing IND. ADMIN. CODE tit. 45, r. 4.1-3-5(b)(4) (1996)).
614. *Id.*
615. *Id.* (quoting IND. ADMIN. CODE tit. 45, r. 4.1-3-5(b)(3) (1996)).
616. *See id.* (citing IND. ADMIN. CODE tit. 45, r. 4.1-3-5(e) (1996)).

federal regulations applicable to QTIP elections.[617] Under the federal regulations, a second filing of an inheritance return could be used in making the QTIP election so long as the second return was filed within the time when the inheritance return could be filed, which the estate did in this case.[618] However, the IDSR pointed out that a QTIP election "'cannot be made on an amended inheritance tax return.'"[619] The estate countered, stating that it filed a supplemental inheritance tax return and not an "amended" inheritance tax return, arguing that a supplemental return is one filed before the due date of the return.[620] However, the court found that the intent of the regulation, which has the force of law, was that failure to attach a QTIP election to the initial inheritance tax return must result in not treating the transfer as a QTIP transfer.[621] Though the court sympathized with the estate's position, it held that the estate had failed to file a valid QTIP election.[622]

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617. *See id.*
618. *See id.*
619. *Id.* (quoting IND. ADMIN. CODE tit. 45, r. 4.1-3-5(c) (1996)).
620. *See id.* at 511.
621. *Id.* (citing IND. ADMIN. CODE tit. 45, r. 4.1-3-5(e) (1996)).
622. *Id.*

RECENT DEVELOPMENTS IN INDIANA TORT LAW

TAMMY J. MEYER*
KYLE A. LANSBERRY**

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INTRODUCTION

From October 1997 to October 1998, federal and state appellate courts of Indiana were presented with novel and complex issues in the area of Indiana tort law. They were called upon to decide issues of first impression in the State of Indiana, as well as to re-examine long-standing judicial precedent. Their decisions in this area reflect both the dynamic nature of tort law in general, and the broad range of areas in which it affects our society as a whole.

I. NEGLIGENCE

A. Defining the Scope of the Duty Owed

1. Abrogation of the Latent/Patent Distinction as the Basis for

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* Lewis & Wagner, Indianapolis. B.S., *summa cum laude*, 1986, Indiana Wesleyan University; J.D., *summa cum laude*, 1989, Indiana University School of Law—Indianapolis.

** Lewis & Wagner, Indianapolis. B.S., *cum laude*, 1995, Ball State University; J.D., 1998, Indiana University School of Law—Indianapolis.

Determination of a Legal Duty to Inspect.—In *McGlothlin v. M & U Trucking, Inc.*,[1] the Indiana Supreme Court was called upon "to address the continued viability of the latent/patent distinction"[2] as a factor in determining the existence of a duty on the part of a supplier of a chattel to be used by another. Specifically, the court addressed the following issue: "When a defective chattel causes personal injury, should the legal duty owed by a supplier of the chattel rest upon whether the defect is considered 'latent' rather than 'patent'?"[3]

This lawsuit arose from an accident that occurred in 1990. The plaintiff was injured during the course of his employment when the landing gear of a semi-trailer into which he was loading televisions collapsed. He sustained serious injuries and sued the owner, lessor and transporter of the trailer, alleging that each of the defendants "'negligently owned, operated and maintained' the trailer,"[4] and that their breach of duty caused his injuries. Specifically, the plaintiff claimed that the defendants' repair and inspection procedures for latent defects were inadequate and that this inadequacy contributed to the collapse of the trailer's landing gear.[5]

The trial court "entered summary judgment against the plaintiff, concluding, *inter alia*, that 'Indiana law did not impose a duty on [the defendants] to discover latent defects.'"[6] On appeal, the Indiana Court of Appeals affirmed the trial court's judgment because it too found that no duty existed as a matter of law.[7] Recognizing that "'no Indiana court ha[d] addressed directly the question of a supplier's liability for injury caused by a latent defect in a chattel furnished for the use of another,'" the appellate court concluded that the defendants "'did not owe [the plaintiff] a duty to detect a latent defect in the landing gear.'"[8]

Shortly after it issued the *McGlothlin* opinion, the court of appeals again faced this issue in *Bloemker v. Detroit Diesel Corp.*[9] The *Bloemker* court was critical of the rationale employed in *McGlothlin*, stating that:

> Defining the duty owed in terms of the nature of the defect overlooks the distinction between the existence of a duty and the breach of that duty. The duty would appear to be one of inspection in the first instance because there is no way of knowing the nature of the defect as latent or patent without inspection.[10]

According to the *Bloemker* court,

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1. 688 N.E.2d 1243 (Ind. 1997).
2. *Id.* at 1244.
3. *Id.* at 1243-44.
4. *Id.* at 1244.
5. *See id.*
6. *Id.*
7. *Id.*
8. *Id.* (quoting McGlothlin v. M & U Trucking, Inc., 649 N.E.2d 135, 139-40 (Ind. Ct. App. 1995)).
9. 655 N.E.2d 117 (Ind. Ct. App. 1995).
10. *Id.* at 123.

> [T]he nature of the defect becomes relevant only when determining whether the duty to inspect was breached. Breach of the duty would arise where a supplier of a chattel fails, upon reasonable inspection, to discover a patent defect. Where a latent defect exists, there would be no breach for failing to discover [it], so long as a reasonable inspection was performed.[11]

However, although the *Bloemker* court disagreed with *McGlothlin*'s latent/patent distinction, it acknowledged the existence of controlling Indiana Supreme Court precedent consistent with *McGlothlin*;[12] precedent that held that "[t]he duty to inspect arises from knowledge of possible defects or their reasonable probability."[13]

The Indiana Supreme Court granted transfer in *McGlothlin* to address the concerns expressed by the *Bloemker* court and to resolve the inconsistencies between the supreme court's broad evaluation of duty as expressed in its recent opinions, and its previous precedent, which narrowly determined duty based solely upon a supplier's knowledge of potential defects.[14]

Relying upon the considerations reflected in the Restatement (Second) of Torts[15] and Indiana jurisprudence regarding the determination of whether a duty exists, the Indiana Supreme Court agreed with the concerns expressed by *Bloemker* and overruled its previous precedent.[16] The court found the employment of the latent/patent distinction to be an unsatisfactory basis for deciding the existence of a legal duty to inspect.[17] It held that while the inquiry into the reasonable discoverability of a defect may be proper in evaluating whether a supplier has breached the duty of reasonable care, it is improper in determining whether such duty exists.[18] To determine whether a duty to inspect exists, the court suggested that Indiana courts should instead focus on those factors explored in typical negligence cases, including: the relationship of the parties, the reasonable foreseeability of harm to the person injured, and public policy concerns.[19]

2. *Mental Capacity as a Factor in the Determination of Duty.*—In *Creasy v. Rusk*,[20] the Indiana Court of Appeals was faced with the novel issue of whether a person's mental capacity must be factored into the determination of whether a legal duty exists. Specifically, the court was called upon to decide whether "a

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11. *Id.*
12. *Id.*
13. Evansville Legion Home Ass'n v. White, 154 N.E.2d 109, 111 (Ind. 1958), *overruled by* McGlothlin v. M & U Trucking, Inc., 688 N.E.2d 1243 (Ind. 1997).
14. *McGlothlin*, 688 N.E.2d at 1245.
15. RESTATEMENT (SECOND) OF TORTS §§ 388, 392 (1965).
16. *McGlothlin*, 688 N.E.2d at 1245.
17. *Id.*
18. *Id.*
19. *Id.*
20. 696 N.E.2d 442 (Ind. Ct. App. 1998).

person institutionalized with a mental disability owes a duty to his caregiver to refrain from conduct that results in injury to the caregiver."[21]

The parties in *Creasy* argued for and against adopting a general rule, used in several other jurisdictions, that mentally disabled individuals are liable for their tortious activities without regard to the individual's mental capacity to control or to understand the consequences of their actions.[22] The same rule is firmly embodied in the Restatement (Second) of Torts, which provides: "Unless the actor is a child, his insanity or other mental deficiency does not relieve the actor from liability for conduct which does not conform to the standard of a reasonable man under like circumstances."[23]

The Indiana Court of Appeals likened this issue to that involving the mental capacity of a child. With regard to children, Indiana courts have generally established the following three tiered analysis, which holds a child to the exercise of care proportionate to the child's capacity:

> (1) children under the age of 7 years are conclusively presumed to be incapable of being contributorily negligent;
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> (2) between the ages of 7 and 14 years of age, a rebuttable presumption exists that a child may be guilty of contributory negligence;
>
> (3) children over the age of 14, absent special circumstances, are chargeable with exercising the standard of care of an adult.[24]

In *Creasy*, the Indiana Court of Appeals determined that Indiana has likewise indicated a willingness to factor in an adult's mental capacity when determining whether to hold an adult person responsible for negligence. Consequently, it held that a person's mental capacity, "whether that person is a child or an adult, must be factored into the determination of whether a legal duty exists."[25]

However, the court cautiously noted that:

> the determination of whether such a duty exists is most frequently accomplished by balancing the following three factors set forth by the Indiana Supreme Court [in] *Webb v. Jarvis*:[26] (1) the relationship between the parties; (2) the reasonable foreseeability of harm to the person injured; and (3) public policy concerns.[27]

Such factors are typically balanced by the court, as a matter of law, rather than left for a jury to decide. Thus, the court suggested that "genuine issues of

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21. *Id.* at 444.

22. *Id.*

23. RESTATEMENT (SECOND) OF TORTS § 283B (1964).

24. *Creasy*, 696 N.E.2d at 445 (citing Bailey v. Martz, 488 N.E.2d 716, 721 (Ind. Ct. App. 1986); Smith v. Diamond, 421 N.E.2d 1172, 1177-79 (Ind. Ct. App. 1981)).

25. *Id.* at 446.

26. 575 N.E.2d 992, 995 (Ind. 1991).

27. *Creasy*, 696 N.E.2d at 446.

material fact may be frequently interwoven with the relationship and foreseeability factors, making the existence of a duty a mixed question of law and fact, ultimately to be decided by the finder of fact."[28]

In determining whether a relationship exists between two parties upon which a legal duty may be based, the *Creasy* court noted that "there must be some knowledge on the part of the purported tortfeasor that his or her conduct may draw him or her into a legal relationship with another."[29] The court found that "[i]n the absence of extenuating circumstances, the relationship between a patient in a health care facility and the caregivers working in the facility is sufficient upon which to base a legal duty."[30]

However, the court established that extenuating circumstances that may alter the relationship between parties include the patient's mental capacity, and that such a relationship may "vary according to the nature and extent of the individual's mental capacity to control his actions and understand the consequences thereof."[31] Thus, the court found that the greater the degree of the individual's impairment, the less weight will typically be given to the relationship factor in determining a legal duty.[32]

The court also noted that the foreseeability factor is typically analyzed by considering broadly the type of plaintiff and harm involved, without regard to the facts of the actual occurrence.[33] The type of plaintiff involved in this case was a caregiver of patients with Alzheimer's disease. Because such patients often exhibit signs of violence and combativeness, the court found it was foreseeable that when an Alzheimer's patient becomes combative in the presence of his caregiver, the caregiver will be injured. Accordingly, the court concluded that "the foreseeability factor weighs in favor of imposing a duty."[34]

Finally, the court in *Creasy* was faced with the issue of the public policy concerns involved in imposing a duty upon those with a diminished mental capacity—a source of passionate debate throughout the United States.[35] The court recognized the pros and cons of imposing a duty on institutionalized mentally disabled individuals; factors that have been litigated in jurisdictions across the country.[36] However, like the relationship factor, the court concluded that the public policy implications of imposing a duty on an institutionalized mentally disabled patient are dependent upon the degree of the person's incapacity.[37] Thus, the court suggested that the greater the individual's degree of impairment, the more public policy concerns weigh against imposing a duty

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28. *Id.*
29. *Id.* (citing T.S.B. by Dant v. Clinard, 553 N.E.2d 1253 (Ind. Ct. App. 1990)).
30. *Id.*
31. *Id.*
32. *Id.*
33. *Id.* (citing Goldsberry v. Grubbs, 672 N.E.2d 475, 479 (Ind. Ct. App. 1996)).
34. *Id.*
35. *Id.*
36. *Id.* at 447.
37. *Id.*

upon the individual.[38]

Concluding that genuine issues of material fact existed in this case concerning the degree of the defendant's impairment and, accordingly, the existence of a legal duty, the court found that summary judgment was precluded.[39] The court suggested, however, that the degree of a patient's impairment may be established by the affidavit of an expert who is qualified to testify to the extent of an individual's dementia and its effect on his ability to control his actions or understand the consequences thereof.[40]

3. Duty of Care of Children Between the Ages of Seven and Fourteen.—In *Maynard v. Indiana Harbor Belt Railroad*,[41] the District Court for the Northern District of Indiana decided an issue of substantive Indiana law that has produced conflicting appellate court decisions. Specifically, the court decided "whether Indiana has a presumption as to a child's capacity to exercise care and discretion."[42]

The case involved a thirteen-year-old boy who was injured while climbing between railroad cars owned by the defendant. The defendant moved for summary judgment on the basis that the child was a trespasser and that, under Indiana law, it did not breach the duty of care owed to a trespasser.[43] The court found that the child was indeed a trespasser on the property at the time of his injury, and that if he were an adult the railroad company would "owe him no duty except to refrain from wilfully or intentionally injuring him after discovering his presence."[44] Because the plaintiffs claimed only negligence, and provided no evidence of intent to harm the child, the court found that, under the general rule, the claim would be dismissed.[45]

However, because the plaintiff was only thirteen years old at the time of the accident, the court determined that he may fall under the exception to the general rule that a railroad company does not have a duty to anticipate a trespasser and may assume that there are no trespassers on its property.[46] This exception was first enunciated in *Cleveland C., C. & St. L. Railway v. Means*,[47] where the Indiana Court of Appeals held:

> Where the person on the track is a child non sui juris of whose presence the railroad company has knowledge, actual or constructive . . . the company must operate its cars on such tracks with reference to the probable presence of such child and use some care to avoid injuring it;

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38. *Id.* at 447-48.
39. *Id.* at 448.
40. *Id.*
41. 997 F. Supp. 1128 (N.D. Ind. 1998).
42. *Id.* at 1132.
43. *See id.* at 1128.
44. *Id.* at 1132.
45. *Id.*
46. *Id.* at 1131-32 (citing Freitag v. Chicago Junction Ry., 89 N.E. 501 (Ind. App. 1909)).
47. 104 N.E. 785 (Ind. App. 1914).

> otherwise no additional care is imposed on the company over that which it owes the adult trespasser on its tracks.[48]

The *Maynard* court defined the term "non sui juris" as "lacking legal capacity to act for oneself, as in the case of a minor or mentally incompetent person."[49] It further found that where a child is sui juris, it is held to be capable of exercising some care and discretion, but it is not necessarily held to the same degree of care required of a person of mature years.[50] Thus, the district court was forced to look to Indiana law to determine the status of the presumption as to a child's capacity.[51]

The plaintiffs argued that children between the ages of seven and fourteen are presumed to be non sui juris, or incapable of exercising some care and discretion. The defendant countered that these children are presumed to be sui juris, or capable of exercising some care and discretion.[52] Both parties cited valid Indiana case law in support of their respective positions, and the court found that whether Indiana has a presumption as to a child's capacity to exercise care and discretion is unclear.[53] Specifically, the court noted that no Indiana Supreme Court case is directly on point regarding this issue, and that Indiana's intermediate courts have taken contrasting positions.[54]

For example, the Fourth District of the Indiana Court of Appeals has made the conclusory statement that for children between the ages of seven and fourteen "a rebuttable presumption exists that they *may be guilty* of negligence."[55] However, the Second and Third Districts of the Indiana Court of Appeals have stated that children between the ages of seven and fourteen are rebuttably presumed *incapable* of negligence.[56] Thus, because the appellate court decisions conflict on this issue, the *Maynard* court looked to the language of the cases and the laws of other states for guidance.[57]

Based upon its analysis of this law, the District Court for the Northern District of Indiana concluded that it believed that the Indiana Supreme Court would not find that children between the ages of seven and fourteen are rebuttably presumed to be capable of exercising some discretion and care.[58] The court was less certain as to whether the Indiana Supreme Court would rebuttably presume that children between the ages of seven and fourteen are incapable of

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48. *Id.* at 792.
49. *Maynard*, 997 F. Supp. at 1132 (citing BLACK'S LAW DICTIONARY 1058 (6th ed. 1990)).
50. *Id.* (citing Cole v. Searfoss, 97 N.E. 345, 348 (Ind. App. 1912)).
51. *Id.*
52. *See id.*
53. *See id.*
54. *Id.* at 1133-34 (citations omitted).
55. Bailey v. Martz, 488 N.E.2d 716, 721 (Ind. Ct. App. 1986) (emphasis added).
56. Brockmeyer v. Fort Wayne Pub. Transp., 614 N.E.2d 605, 607 (Ind. Ct. App. 1993); Baller by Baller v. Corle, 490 N.E.2d 382, 385 (Ind. Ct. App. 1986).
57. *Maynard*, 997 F. Supp. at 1134.
58. *Id.* at 1134-35.

exercising discretion and care, or would reject any presumption.[59] However, the court held that because the question of a particular child's ability to appreciate the danger is generally a question of fact for the jury, it would not grant the defendant's motion for summary judgment even if the Indiana Supreme Court found that there was no presumption.[60]

4. *Duties of Suppliers and Transporters of Natural Gas.*—In *Downs v. Panhandle Eastern Pipeline Co.*,[61] plaintiffs were customers of a local gas utility company whose house exploded following a natural gas leak from the utility's pipe. They sued the utility, the supplier of the natural gas, and the transporter of the gas for negligence and negligent entrustment. Specifically, the plaintiffs argued that the supplier, Vesta, and the transporter, Panhandle, were negligent in supplying and transporting the gas.[62] Both defendants moved for summary judgment, claiming that their respective liability ended once the gas was delivered to the utility and that they had no duty to investigate the condition of the service lines.[63]

At the outset, the Indiana Court of Appeals noted that natural gas is, as a matter of law, a dangerous substance.[64] However, it further noted that the utility of natural gas is derived from the very qualities that make it dangerous.[65] Thus, to succeed in her negligence claim, the court noted that the plaintiff must demonstrate that the defendants owed her a legal duty.[66]

Relying on the appellate court's decision in *City of Indianapolis v. Bates*,[67] the plaintiff argued that a gas provider is liable for damages caused by the failure of equipment installed and under the control of another party when the provider knows or has reason to know that injury may result from its continued provision of gas.[68] In *Bates*, the defendant gas company had entered the premises and examined and tested all appliances, gas pipes and tubing in the home prior to an explosion. The court held that the gas company had assumed such duties and thereby become responsible for its negligence.[69] However, the court of appeals in *Downs* agreed with the defendants that the plaintiff had misconstrued the holding in *Bates*, finding that "Indiana courts, heretofore, have not determined whether a gas supplier or gas transporter has a duty to a customer of a local gas company to insure that the distribution system of the local gas company is safely

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59. *Id.* at 1135.
60. *Id.* at 1135-36.
61. 694 N.E.2d 1198 (Ind. Ct. App. 1998).
62. *See id.* at 1201.
63. *See id.*
64. *Id.* at 1202 (citing South Eastern Ind. Natural Gas Co., v. Ingram, 617 N.E.2d 943, 952 (Ind. Ct. App. 1993)).
65. *Id.*
66. *Id.*
67. 205 N.E.2d 839 (Ind. App. 1965).
68. *See Downs*, 694 N.E.2d at 1202, 1203.
69. *Bates*, 205 N.E.2d at 847.

maintained and operated."[70]

In deciding whether to impose a common law duty upon the defendants, the court determined that it must employ the balancing test enumerated by the Indiana Supreme Court in *Webb v. Jarvis.*[71] Thus, the *Downs* court weighed the following factors: the relationship between the parties, the reasonable foreseeability of harm to the person injured, and public policy concerns. The court first considered the nature of the relationship, the defendant's knowledge, and the circumstances surrounding the relationship in order to determine whether a relationship exists.[72] Analogizing the determination of duty to that owed by a supplier of electricity, the court held that because the defendants had neither ownership nor control of the defective pipe from which the gas escaped or any other part of the utility's system, there was no relationship between the defendants and the plaintiff that would impose a duty upon the defendants to insure that the utility's distribution system was safe.[73]

The *Downs* court next addressed the factor of foreseeability. In reviewing this factor, it focused on whether the person actually harmed was a foreseeable victim and whether the type of harm actually inflicted was reasonably foreseeable.[74] The court found that the plaintiff's arguments centered around the assertion that the defendants, because of an alleged lack of sophistication of the small utility and its gas distribution system, should have known that the utility's system was unsafe.[75] The court disagreed with the plaintiff's arguments, noting that the designated facts did not support an inference that the plaintiffs or other gas customers inevitably were exposed to the danger of explosion.[76] Moreover, even if the court were to determine the defendants had constructive knowledge of the deficiencies of the utility's system, because of the distant relationship between the defendants and the plaintiff, such constructive knowledge alone would not be enough to impose a duty.[77]

This determination was supported by established precedent in which the court noted that where ownership or control of utility lines is absent, actual knowledge of the circumstances that created an imminent danger to the injured party is required before liability attaches.[78] Relying on this precedent, the court concluded that the defendants would be required to have actual knowledge of an unsafe condition before they would have a duty to take action.[79]

In response, the plaintiff argued that the defendants had a duty to inquire

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70. *Downs*, 694 N.E.2d at 1203.

71. *Id.* (citing Webb v. Jarvis, 575 N.E.2d 687, 688 (Ind. Ct. App. 1991)).

72. *Id.*

73. *Id.* at 1204 (citing Northern Ind. Pub. Serv. Co. ("NIPSCO") v. East Chicago Sanitary Dist., 590 N.E.2d 1067 (Ind. Ct. App. 1992)).

74. *Id.* (citing *Webb*, 575 N.E.2d at 997).

75. *Id.*

76. *Id.* at 1205.

77. *Id.*

78. *Id.* (citing *NIPSCO*, 590 N.E.2d at 1073).

79. *Id.* at 1205.

about or investigate the safety of the utility's distribution system.[80] However, because the defendants did not own or control the distribution system, the court concluded they had no duty to inspect it.[81]

The court finally considered whether there is a public policy reason for imposing a duty of care upon the suppliers and transporters of gas to ensure that utilities to which they supply gas follow the legal requirements for the operation of such a utility and otherwise exercise reasonable care to protect their customers and others.[82] The court noted that while

> there is a strong argument that liability should be imposed on anyone that has within their means to inspect, supervise and oversee the distribution of gas to the public, there is little to be gained by imposing such a duty on one who has no control of or access to the distribution system. The cost of imposing such a duty would exceed the benefit to be gained by requiring the supplier and transporter to obtain access and exercise control in addition to that already in the hands of the utility.[83]

After balancing each of the *Webb* factors, the court concluded "that the [defendants] owed no common law duty to the [plaintiffs]."[84] Likewise, it concluded that the defendants assumed no duty to the plaintiff.[85]

B. Proximate Cause—Basis for Summary Judgment

Proximate cause is rarely a sufficient basis for the entry of summary judgment in a negligence case. However, when an unforeseeable intervening act breaks the line of causation that led to a plaintiff's injury, summary judgment is generally warranted. During the course of this survey period, the Indiana Court of Appeals had an opportunity to examine the type of factual scenario that might warrant the entry of summary judgment based upon the element of proximate cause.

In *Straley v. Kimberly*,[86] a local natural gas distribution company employee brought negligence and negligent entrustment actions against various defendants for injuries sustained from an explosion that occurred while he was attempting to repair a gas main that was ruptured by a subcontractor digging a water line trench with a backhoe.[87] The subcontractor immediately phoned the home construction contractor, informed him of the damaged line and asked him to call the gas company. The contractor then notified the gas company to alert them of the ruptured line. In response, the gas company dispatched a repair crew,

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80. *See id.*
81. *Id.* (citing *NIPSCO*, 590 N.E.2d at 1073).
82. *Id.* at 1205-06.
83. *Id.* at 1206.
84. *Id.*
85. *Id.* at 1206-07.
86. 687 N.E.2d 360 (Ind. Ct. App. 1997).
87. *Id.* at 362-63.

including the plaintiff, to the site. More than an hour after the gas crew assumed control of the repairs the gas ignited, causing the plaintiff's injuries.[88]

The plaintiff's complaint alleged that each of the defendants negligently contributed to the severance of the underground gas line, and that several of the defendants negligently entrusted the water line trench excavation subcontractor to lay the water line.[89] In response, each of the defendants moved for summary judgment, contending that they did not owe the plaintiff a duty of care and that their respective acts were not the proximate cause of the plaintiff's injuries.[90] The trial court granted the defendants' motions for summary judgment, concluding that, as a matter of law, none of the alleged negligent acts were the proximate cause of the plaintiff's injuries.[91]

On appeal, the plaintiff contended that a question of fact existed regarding whether the defendants' acts were the proximate cause of the plaintiff's injuries. Specifically, he argued that the injuries were the foreseeable consequence of the defendants' negligent acts.[92] The defendants countered that although they may have initially caused the gas leak, the gas company's actions in repairing the gas main, including its failure to turn off the gas, were intervening superseding causes of the plaintiff's injuries; therefore, they argued they were not liable as a matter of law.[93]

Initially, the Indiana Court of Appeals noted that in determining whether an act is the proximate cause of another's injury, it considers whether the injury was a natural and probable consequence of the negligent act, which, in light of the attending circumstances, could have been reasonably foreseen or anticipated.[94] Thus, to be considered a proximate cause, the negligent act must have set in motion a chain of circumstances that in natural and continuous sequence lead to the resulting injury.[95] However, the court further noted that the intervention of an independent, superseding negligent act will relieve the original negligent actor of legal liability if that act could not have been reasonably foreseen.[96]

Applying the law to the facts of this case, the *Straley* court found that although the defendants contributed to the severance of the gas main, they merely started a chain of events that eventually led to the plaintiff's injuries.[97] The defendants immediately contacted the gas company to inform it of the leak. The gas company took several unforeseeable steps that broke the chain of causation. Specifically, the court found that the gas company's failure to turn off the gas

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88. *See id.* at 363.
89. *See id.*
90. *See id.*
91. *See id.*
92. *See id.* at 364.
93. *See id.*
94. *Id.* (citing Goldsberry v. Grubbs, 672 N.E.2d 475, 477 (Ind. Ct. App. 1996)).
95. *Id.* (citing City of Portage v. Lindbloom, 655 N.E.2d 84, 86 (Ind. Ct. App. 1986)).
96. *Id.* (citing Lutheran Hosp. of Ind. 126, Inc. v. Blaser, 634 N.E.2d 864, 871 (Ind. Ct. App. 1994)).
97. *Id.* at 364-65.

was an unforeseeable intervening act that broke the line of causation.[98] Therefore, because it concluded that assigning legal liability to the defendants would be inconsistent with the policy underlying proximate cause, the court held, as a matter of law, that the defendants were not the proximate cause of the plaintiff's injuries.[99]

II. The Public Use Exception to Landlord Nonliability

As a general rule in the State of Indiana, in the absence of statute, covenant, fraud or concealment, a landlord who gives a tenant full control and possession of leased property will not be liable for personal injuries sustained by the tenant or other persons lawfully upon the premises.[100] Once possession and control of property have been surrendered, a landlord generally does not owe a duty to protect tenants from defective conditions.[101]

However, Indiana courts have recognized a "public use exception" to the general rule of landlord non-liability. This exception provides:

> "Where premises are leased for public or semi-public purposes, and at [the] time of lease, conditions exist which render premises unsafe for purposes intended, or constitute a nuisance, and landlord knows or by exercise of reasonable care ought to know of conditions, and a third person suffers injury on account thereof, landlord is liable, because [the] third person is there at invitation of landlord, as well as of tenant."[102]

Thus, for the public use exception to apply, a plaintiff must demonstrate that he or she was a third person who was injured because of the existing condition.[103]

In *Smith v. Standard Life Insurance Co.*,[104] the Indiana Court of Appeals was faced with the following issue of first impression: Whether an employee of a tenant qualifies as a "third person" under the public use exception to the general rule of non-liability for landlords.[105] In *Smith*, the plaintiff, an employee of Hook's Drugs, was injured when she slipped and fell on an icy sidewalk outside of a Hook's store. She filed suit against Standard Life, the owner and lessor of the premises, alleging that the defendant had breached its duty of reasonable care when it knew or should have known at the time of the lease that a dangerous condition existed on the premises, specifically that a drain spout directed water onto the sidewalk in a concentrated area, causing ice to form. The plaintiff also alleged that Standard Life was negligent because it failed to remove

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98. *Id.* at 365.

99. *Id.*

100. *See* Rogers v. Grunden, 589 N.E.2d 248, 254 (Ind. Ct. App. 1992).

101. *See id.*

102. Walker v. Ellis, 129 N.E.2d 65, 73 (Ind. App. 1955) (quoting Fraser v. Kruger, 298 F. Supp. 693, 696-97 (8th Cir. 1924)).

103. *See id.*

104. 687 N.E.2d 214 (Ind. Ct. App. 1997).

105. *Id.* at 216.

accumulations of snow and ice from the sidewalk.[106]

Standard Life had relinquished complete possession and control of the premises to Hook's, which accepted the premises in its condition at the time of the lease and agreed to keep the premises in good condition and repair. In fact, Hook's employees were responsible for snow and ice removal from the sidewalk directly in front of Hook's.[107]

In response to the defendant's motion for summary judgment, the plaintiff asserted that summary judgment should be precluded because the "public use exception" to the general rule of landlord non-liability applied and created a duty owed by the defendant to the plaintiff. Specifically, the plaintiff argued that she qualified as a "third person" protected by the public use exception because her injury occurred on the sidewalk outside of the area occupied by Hook's, rather than inside the store.[108] The defendant countered that the plaintiff was injured during the course of her employment and did not qualify as a third person under the exception.[109]

The Indiana Court of Appeals agreed with the defendant and affirmed the trial court's entry of summary judgment.[110] Adopting the Restatement (Second) of Torts' definition of who qualifies as a "third person" under the public use exception, the court held, as a matter of first impression, that "third persons" include:

> [A]ll persons other than the possessor of the land, or his servants acting within the scope of their employment. It includes such servants when they are acting outside of the scope of their employment, as well as other invitees or licensees upon the premises, and also trespassers on the land, and even persons outside of the land whose acts endanger the safety of the visitor.[111]

The court concluded that the plaintiff, a Hook's employee, failed to meet the "third person" requirement of the public use exception and that the exception, therefore, did not apply.[112]

III. COMPARATIVE FAULT

In *Edwards v. Sisler*,[113] the Indiana Court of Appeals was faced with the issue of whether Indiana's Comparative Fault Act[114] abrogated the common law rule that a tort-feasor may not rely on a physician's negligent treatment of a victim's

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106. *See id.*
107. *See id.* at 217.
108. *See id.* at 217-18.
109. *See id.* at 218.
110. *Id.*
111. *Id.* (citing RESTATEMENT (SECOND) OF TORTS § 344 cmt. b (1965)).
112. *Id.*
113. 691 N.E.2d 1252 (Ind. Ct. App. 1998).
114. IND. CODE §§ 34-51-2-1 to -19 (1998) (formerly IND. CODE §§ 34-4-33-1 to -12 (1993)).

injuries to avoid or reduce the tortfeasor's liability.[115] The plaintiff was injured in an automobile accident, and filed suit against the driver of the other car and his employer. After deposing the plaintiff, the defendants' counsel learned that the physician who treated the plaintiff for the injuries she sustained in the collision had performed a surgical procedure on the wrong leg.[116] The defendants then moved to amend their answer to include a claim that the plaintiff's damages were caused in full or in part by a nonparty pursuant to section 34-4-33-10(a) of the Indiana Code, within the Comparative Fault Act.[117]

The plaintiff objected to this amendment and urged the trial court to determine that the Indiana Court of Appeals' reasoning in *Whitaker v. Kruse*[118] survived the adoption of Indiana's Comparative Fault Act. In *Whitaker*, the court held clearly erroneous a jury instruction that stated, in essence, that a plaintiff could not recover for injuries if the evidence indicated that her physicians had misdiagnosed and/or mistreated her injuries.[119] The *Whitaker* court further adopted the general rule of the Restatement (Second) of Torts, which provides:

> If the negligent actor is liable for another's bodily injury, he is also subject to liability for any additional bodily harm resulting from normal efforts of third persons in rendering aid which the other's injury reasonably requires, irrespective of whether such acts are done in a proper or a negligent manner.[120]

However, the *Edwards* trial court disagreed with the plaintiff's argument, and allowed the defendants' proposed amendment.[121]

On interlocutory appeal, the plaintiff urged the appellate court to determine that the *Whitaker* decision survived adoption of the Comparative Fault Act. In addition, the plaintiff relied upon *Holden v. Balko*,[122] a federal decision construing Indiana law. Addressing precisely the question at issue in *Edwards*, the District Court for the Southern District of Indiana in *Holden* found that a defendant could not name a health care provider as a nonparty to whom fault could be attributed.[123] *Holden* determined that Indiana's Comparative Fault Act did not supplant the long-standing rule in Indiana that an original tortfeasor is responsible for the subsequent negligence of a health care provider who treats the plaintiff's injuries.[124]

In response, the defendant argued that the *Holden* rule was necessarily changed by Indiana's adoption of comparative fault in tort claims, which allows

115. *Edwards*, 691 N.E.2d at 1254.
116. *See id.* at 1253.
117. *See id.*
118. 495 N.E.2d 223 (Ind. Ct. App. 1986).
119. *Id.* at 227.
120. *Id.* at 225 (citing RESTATEMENT (SECOND) OF TORTS § 457 (1965)).
121. *Edwards*, 691 N.E.2d at 1253.
122. 949 F. Supp. 704 (S.D. Ind. 1996).
123. *Id.* at 714.
124. *Id.* at 710-14.

a defendant to assert an affirmative defense "'that the damages of the claimant were caused in full or in part by a nonparty.'"[125] Essential to the defendant's argument was the assertion that the Comparative Fault Act seeks to attribute fault proportionally to those actors who contributed to the damages.[126] The *Edwards* court, however, disagreed with the defendant's interpretation.[127]

The *Edwards* court found it significant that the overriding reason for adoption of the Comparative Fault Act was to "ameliorate the harshness of the former rule of contributory negligence which would not allow a slightly blameworthy plaintiff any recovery."[128] Moreover, it found the reasoning of *Holden* instructive. As noted in *Holden* and adopted by the Indiana Court of Appeals, "it is not intended that the [Comparative Fault A]ct will foster additional lawsuits."[129]

Thus, the court found that "while a plaintiff may choose to sue a negligent caregiver, the plaintiff should not be required to do so, nor should the decision be one made by the defendant,"[130] because "[a] stranger to the physician-patient relationship should not have a stake in scouring an injured party's medical records searching for some act of malpractice or negligence in order to extricate himself from all or some portion of the damages to the injured party."[131] Accordingly, the appellate court reversed the decision of the trial court to allow the amendment to add the non-party defense.[132]

IV. STATUTE OF LIMITATIONS AND THEORY OF RECOVERY

Statutes of limitations are favored by courts and litigants because they afford security against stale claims and promote the peace and welfare of society.[133] "They are enacted upon the presumption that one having a well-founded claim will not delay in enforcing it."[134] Thus, our courts have consistently held that the defense of a statute of limitations is important to the efficient administration of justice.

By statute, claims for personal injuries must be brought within two years of accrual or they are deemed time-barred.[135] In a recent case, *Schuman v.*

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125. *Edwards*, 691 N.E.2d at 1254 (quoting IND. CODE § 34-4-33-2 (1993)).

126. *See id.*

127. *Id.* at 1255.

128. *Id. See also* Indianapolis Power v. Snodgrass, 578 N.E.2d 669, 672 (Ind. 1991).

129. *Edwards*, 691 N.E.2d at 1255 (citing *Holden*, 949 F. Supp. at 712).

130. *Id.* (citing *Holden*, 949 F. Supp. at 712).

131. *Id.* (citing *Holden*, 949 F. Supp. at 711-12).

132. *Id.*

133. *See* A.M. v. Roman Catholic Church, 669 N.E.2d 1034, 1037 (Ind. Ct. App. 1996) (citing Shideler v. Dwyer, 417 N.E.2d 281, 283 (Ind. 1981)).

134. *Id.* (citing *Shideler*, 417 N.E.2d at 283).

135. Indiana Code section 34-11-2-4 (1998), formerly Indiana Code section 34-1-2-2 (1993), provides, in relevant part: "An action for: (1) injury to person . . . must be commenced within two (2) years after the cause of action accrues." IND. CODE § 34-11-2-4 (1998).

Kobets,[136] the Indiana Court of Appeals sent a clear message that the theory of recovery advanced in a complaint will not control for purposes of determining the appropriate statute of limitations. Rather, courts must look to the nature or substance of the cause of action to make this determination.[137]

In *Schuman*, the plaintiff brought suit against her landlord in 1996 under a theory of breach of implied warranty of habitability to recover damages for personal injuries.[138] The plaintiff contracted histoplasmosis, a fungal infection, in 1990 from exposure to pigeon droppings in the window casing and wall of her apartment. She had complained to her landlord on numerous occasions that repairs were necessary to keep the pigeons out. However, despite repeated assurances to do so, the landlord neglected to make the needed repairs.[139]

The defendant in *Schuman* moved for judgment on the pleadings, arguing that the plaintiff's claim, though brought under the theory of breach of implied warranty of habitability, was subject to the two-year statute of limitations for personal injuries under section 34-1-2-2 of the Indiana Code.[140] The trial court agreed, and granted the motion.[141] On appeal, the plaintiff argued that the six-year statute of limitations found in Indiana Code section 34-1-2-1[142] applied to her case because her theory of recovery was based on a breach of the oral lease contract and/or breach of an implied warranty of habitability, which also arose out of the oral contract.[143]

However, the appellate court disagreed.[144] The *Schuman* court noted that the general rule is that the nature or substance of the cause of action determines the applicable statute of limitations.[145] "For purposes of determining the appropriate statute of limitations, the substance of a cause of action is ascertained by an inquiry into the nature of the alleged harm and not by reference to the theories

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136. 698 N.E.2d 375 (Ind. Ct. App. 1998).

137. *See id.* at 378.

138. *Id.* at 377.

139. *See id.*

140. IND. CODE § 34-1-2-1 (1993) (recodified at IND. CODE § 34-11-2-4 (1998), without substantive changes).

141. *See Schuman*, 698 N.E.2d at 377.

142. IND. CODE § 34-1-2-1 (1993) (recodified at IND. CODE § 34-11-2-4 (1998) without substantive changes). That section provided:

> The following actions must be commenced within six (6) years after the cause of action accrues. (1) Actions on accounts and contracts in writing. (2) Actions for use, rents, and profits of real property. (3) Actions for injuries to property other than personal property, damages for detention of personal property and for recovering possession of personal property. (4) Actions for relief against frauds.

Id.

143. *See Schuman*, 698 N.E.2d at 378.

144. *Id.* at 378-79.

145. *Id.* at 378 (citing INB National Bank v. Morgan Elec. Serv., Inc., 608 N.E.2d 702, 706 (Ind. Ct. App. 1993)).

of recovery advanced in the complaint."[146] Accordingly, the court held that "the nature of the harm suffered by the plaintiff was clearly injury to her person"[147] and that the trial court therefore correctly determined that the two-year statute of limitations applied.

V. Negligent Infliction of Emotional Distress

A. Indiana's Modified Impact Rule

During the course of this survey period, the Indiana Court of Appeals rendered several decisions interpreting the "direct impact" requirement necessary to recover for claims of negligent infliction of emotional distress under Indiana's modified impact rule. Generally, the tort of negligent infliction of emotional distress depends upon judicial interpretation of whether the plaintiff sustains a direct impact. To fully comprehend the nature of this requirement of the modified impact rule, it is necessary to begin with an analysis of its origin.

Under Indiana's traditional impact rule, damages for mental distress could only be recovered when the distress was accompanied by and resulted from a physical injury caused by a direct impact to the plaintiff.[148] This rule provided that the only emotional trauma compensable under a negligence theory was that arising out of a plaintiff's own injuries.[149] Thus, to recover under the rule, the plaintiff was required to prove that the mental injury was the natural and direct result of the physical injury.[150]

In 1991, the Indiana Supreme Court, in *Shuamber v. Henderson*,[151] modified this traditional impact rule in actions for mental or emotional distress. In *Shuamber*, a drunk driver collided with an automobile, carrying a mother and her two children. As a result of the accident, one of the children was killed.[152] The mother and daughter filed suit against the defendant driver, seeking damages for the emotional distress they suffered from watching the child die. The Indiana Supreme Court noted that the plaintiffs were clearly precluded from recovering damages for their mental injuries under Indiana's traditional impact rule.[153] However, the court modified the traditional impact rule and allowed the plaintiffs to recover.[154]

In *Shuamber*, the Indiana Supreme Court removed as a requirement to sustain an action for negligent infliction of emotional distress, contemporaneous physical injury accompanying the impact, and announced the following modification to

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146. *Id.* (citing Whitehouse v. Quinn, 477 N.E.2d 270, 274 (Ind. 1985)).
147. *Id.*
148. *See* Shuamber v. Henderson, 579 N.E.2d 452, 454 (Ind. 1991).
149. *See id.* (citing Boston v. Chesapeake & O. Ry., 61 N.E.2d 326, 327 (Ind. 1945)).
150. *See id.*
151. 579 N.E.2d 452, 456 (Ind. 1991).
152. *See id.* at 453.
153. *Id.* at 455.
154. *Id.* at 454-56.

the traditional impact rule:

> When as here, a plaintiff sustains a *direct impact* by the negligence of another and, by virtue of that direct involvement sustains an emotional trauma which is serious in nature and of a kind and extent normally expected to occur in a reasonable person, we hold that such a plaintiff is entitled to maintain an action to recover for that emotional trauma without regard to whether the emotional trauma arises out of or accompanies any physical injury to the plaintiff.[155]

In its reexamination of the impact rule, the court reviewed and rejected the traditional reasons for requiring a physical injury to a plaintiff before recovery was allowed: "(1) fear that a flood of litigation will result if claims of this nature are allowed; (2) concern that fraudulent claims will be made (and rewarded); and (3) difficulties in proving a causal connection between the negligent conduct and the emotional distress."[156] The court noted that the presence of physical injury does not make mental damages less speculative and that the presence or absence of mental damage is properly judged by the jury.[157]

B. Judicial Determination of Direct Impact

Since *Shuamber*, the Indiana Court of Appeals has stated that the modified impact rule "'maintains the requirement that [the plaintiff] demonstrate that she suffered a direct physical impact.'"[158] In the past year, the appellate court was faced with several significant cases in which the court determined whether the factual circumstances gave rise to a "physical impact" necessary to maintain a cause of action for negligent infliction of emotional distress.

In *Conder v. Wood*,[159] a pedestrian was attempting to cross a street with a companion when the companion was struck and fatally injured by a truck that was negotiating a turn. The plaintiff had seen that the truck was not going to stop and jumped out of its path. She attempted to pull her companion back; however, before she had time to react, the front wheel of the truck struck her companion and knocked her violently to the ground.[160] The truck continued to roll directly next to where the plaintiff was standing and in the direct path of her fallen companion. Afraid that the truck would run her over, the plaintiff began pounding on the panels of the truck trailer to get the driver's attention. The truck came to a stop just before the rear tire ran over her companion's head; nevertheless, the companion died at the scene.[161]

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155. *Id.* at 456 (emphasis added).

156. *Id.* at 454. *See also* Ross v. Cheema, 696 N.E.2d 437, 439 (Ind. Ct. App. 1998).

157. *Shuamber*, 579 N.E.2d at 454.

158. Etienne v. Caputi, 679 N.E.2d 922, 926 (Ind. Ct. App. 1997) (quoting Gorman v. I & M Electric Co., 641 N.E.2d 1288, 1290 (Ind. Ct. App. 1994)).

159. 691 N.E.2d 490 (Ind. Ct. App. 1998).

160. *See id.* at 491.

161. *See id.*

As a result of the incident, the plaintiff sustained bruises on her arm, emotional and psychological trauma, stress-related headaches, insomnia and personality changes.[162] The plaintiff subsequently filed suit against the truck driver and the trucking company, seeking recovery for her emotional injuries under a theory of negligent infliction of emotional distress.[163] The defendants filed a motion for summary judgment, arguing that any recovery sought by the plaintiff for emotional distress or psychological damage was precluded under Indiana law.[164] The trial court issued an order denying summary judgment.[165]

On appeal, the defendants argued that the modified impact rule announced in *Shuamber v. Henderson*[166] precluded the plaintiff from recovering damages.[167] Interpreting the Indiana Supreme Court's *Shuamber* decision, the Indiana Court of Appeals remarked that it must determine whether the plaintiff suffered a direct physical impact by the negligence of the defendant truck driver.[168] The *Conder* court found that the only physical impact between the plaintiff and the truck driven by the defendant was initiated through the plaintiff's own actions, and not directly through the truck driver's negligence.[169] Thus, the court held that while it was clear that the plaintiff was involved in the incident that resulted in her companion's death, she did not suffer a "'direct physical impact by the negligence of another' necessary for the application of the modified impact rule."[170]

In *Holloway v. Bob Evans Farms, Inc.*,[171] the court of appeals was asked to determine whether the consumption of food that had been cooked with a worm constituted a direct physical impact under the modified impact rule. The plaintiff had consumed approximately one-half of her meal when she discovered that a worm had been cooked with her food.[172] As a result, she experienced vomiting and diarrhea. She also had nightmares about discovering the worm in her food, experienced weight loss and visited both a doctor and a psychologist.[173]

The plaintiff brought suit against the defendant restaurant seeking recovery for her mental and emotional injuries under a theory of negligence. The defendant moved for summary judgment, which the trial court granted.[174] On appeal, the plaintiff claimed that she was entitled to pursue recovery for her

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162. *See id.*
163. *See id.* at 492.
164. *See id.*
165. *See id.*
166. 579 N.E.2d 452 (Ind. 1991).
167. *Conder*, 691 N.E.2d at 492.
168. *Id.* at 493.
169. *Id.*
170. *Id.*
171. 695 N.E.2d 991, 996 (Ind. Ct. App. 1998).
172. *See id.* at 993.
173. *See id.*
174. *See id.*

emotional damages under Indiana's "modified impact rule."[175] In response, the defendant argued that the emotional distress claim must fail because there was no evidence she suffered a direct physical impact required to recover damages for negligent infliction of emotional distress.[176] The plaintiff argued that eating a portion of food that had been cooked with a worm constituted a direct physical impact under the modified impact rule, and the court agreed.[177]

The *Holloway* court found that although the worm was not submitted as evidence or made part of the record, the parties did not dispute that a worm had been cooked and served with the plaintiff's meal.[178] The court noted that had the plaintiff discovered the worm before she began eating, there would have been no direct impact under the modified impact rule.[179] However, it concluded that because she had consumed over one-half of the dinner before she observed the worm fall from her fork, and thus ingested food in which the worm had been cooked, she sustained a direct impact as required by Indiana's modified impact rule.[180]

One day after the court of appeals' decision in *Holloway*, the appellate court rendered another decision on whether certain factual circumstances gave rise to a "physical impact" necessary to maintain an action for negligent infliction of emotional distress. In *Dollar Inn, Inc. v. Slone*,[181] a guest sued a hotel in which she had stayed for negligent infliction of emotional distress associated with her fear of contracting AIDS after she was stabbed in the thumb by a hypodermic needle concealed in the center tube of a toilet paper roll. Following the stabbing, a member of the hotel's staff informed the plaintiff that the needle was probably from an intravenous drug user on the hotel staff.[182] Because she feared possible exposure to disease from the needle, the plaintiff went to the hospital for blood tests. There she was informed by her examining physician that she would need to be tested regularly for AIDS for up to ten years.[183]

When the plaintiff returned home, she was visibly upset, crying, shaking and pale. As a result of her fear of contracting AIDS, she began having problems sleeping, became severely withdrawn, and her relationship with her daughters deteriorated.[184] She took precautions to prevent the possible exposure of her daughters to the disease, such as wearing two pairs of food handler's gloves while cooking and washing her laundry separately. During the two years following the incident she was tested for AIDS every six months, and for the following three years she was tested annually. Fortunately, the plaintiff did not

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175. *See id.* at 996.
176. *See id.*
177. *Id.*
178. *Id.*
179. *Id.*
180. *Id.*
181. 695 N.E.2d 185 (Ind. Ct. App. 1998).
182. *See id.* at 186.
183. *See id.* at 190.
184. *See id.* at 186-87.

test positive for the virus.[185]

The plaintiff filed a complaint against the hotel for the mental suffering associated with the needle stab. Seven years later, her suit finally went to trial and the jury returned a verdict in her favor.[186] On appeal, the defendant contended that the trial court erred by denying its motion for judgment on the evidence, arguing that the plaintiff was required to prove that she was actually exposed to AIDS to recover.[187] The plaintiff countered that actual exposure is not required under Indiana law and that there was sufficient evidence to support the jury's verdict.[188]

The Indiana Court of Appeals noted that to succeed on her claim, the plaintiff "was required to show that she sustained a direct impact as a result of [the defendant's] negligence and as a result of this direct impact suffered an emotional trauma 'which is serious in nature and of a kind and extent normally expected to occur in a reasonable person . . . .'"[189] However, it held that the plaintiff was able to prove an impact other than actual exposure because the needle stab to her thumb was a direct impact, thus satisfying the requirements established by the Indiana Supreme Court in *Shuamber*.[190]

The defendant also claimed that the needle stab was so insignificant that it could not be considered a direct impact.[191] The plaintiff responded that an impact "need not be of a substantial and permanent nature to satisfy the requirement of a direct impact."[192] Relying upon its own precedent, the court found that "'[t]here is no requirement that the injury be severe to support the parasitic mental anguish claim.'"[193] Because the direct impact need not be substantial or permanent in nature, the court held that the needle stab, a physical injury that broke the skin of the plaintiff's thumb, was evidence of a direct impact and satisfied the requirements of the modified impact rule.[194]

Less than three weeks following the *Slone* decision, the court of appeals rendered what may have been its most delicate interpretation of the physical impact requirement. In *Ross v. Cheema*,[195] a homeowner sued a deliveryman and his employer for negligent infliction of emotion distress arising out of an incident in which the deliveryman repeatedly and loudly pounded on the homeowner's door and broke her door knob in an attempt to delivery a letter. On the date of the incident, the plaintiff was in her living room when the doorbell rang. "Before she could answer the door there was a 'tremendous pounding' on the door. She

185. *See id.* at 187.
186. *See id.*
187. *See id.* at 188.
188. *See id.*
189. *Id.* (quoting Shuamber v. Henderson, 579 N.E.2d 452, 456 (Ind. 1991)).
190. *Id.* at 189.
191. *See id.*
192. *Id.*
193. *Id.* (quoting Kroger Co. v. Beck, 375 N.E.2d 640, 643 n.1 (Ind. App. 1978)).
194. *Id.*
195. 696 N.E.2d 437 (Ind. Ct. App. 1998).

heard the locked screen door pop open, then the door knob on the inner door began to twist back and forth,"[196] followed by more pounding. The plaintiff then

> went to a window and saw a car which she did not recognize. Fearful of an intruder, [she] placed a steak knife in her pants for protection before returning to the door. [The plaintiff] opened the front door and a man reached in and put a clipboard in front of her face and told her to sign.[197]

The plaintiff signed the document, but noticed that her screen door lock was broken and the main door knob was hanging by two screws.

As a result of this incident, the plaintiff filed suit claiming that she suffered mental injury that required medical treatment.[198] The defendant moved for summary judgment claiming that the Indiana impact rule barred her recovery, and the trial court agreed.[199]

On appeal, the plaintiff contended that she should be allowed to maintain her action for negligent infliction of emotional distress without regard to whether the emotional trauma was accompanied by any physical injury, because the emotional distress was a "foreseeable consequence" of the defendant's actions.[200] In response, the defendant contended that the plaintiff did not meet the requirements of the modified impact rule under *Shuamber v. Henderson*[201] and that the plaintiff's alleged distress was not reasonable and consequently did not satisfy the reasonableness test in *Shuamber* either.[202]

After carefully analyzing the language of *Shuamber*, the *Ross* court noted that *Shuamber* requires a "direct impact" and a "direct involvement," and that the plaintiff satisfied both conditions.[203] Reasoning that the plaintiff was in her home sitting in her living room when the defendant broke her screen door and began pounding on the main door and twisting the handle vigorously, the court saw no meaningful distinction between a violent impact with an automobile in which one is riding and one with a home in which one is sitting.[204] In both instances, the court held that resulting emotional trauma should be readily foreseen.[205]

In addition to the "direct impact" and "direct involvement" requirements, the *Ross* court also found that *Shuamber* imposes a "reasonableness" requirement.[206] The defendant contended that the plaintiff could not satisfy this requirement because it was unreasonable for the plaintiff to suffer emotional trauma based on

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196. *Id.* at 438.
197. *Id.*
198. *See id.*
199. *See id.*
200. *See id.*
201. 579 N.E.2d 452 (Ind. 1991).
202. *See Ross*, 696 N.E.2d at 438.
203. *Id.* at 439.
204. *Id.*
205. *Id.*
206. *Id.*

his actions.[207] However, the court held that the reasonableness of the plaintiff's injuries was a question of fact for the jury, and that from the designated facts a jury could conclude that the plaintiff, fearful that her home was being broken into, could reasonably experience emotional trauma that the defendant should have foreseen.[208]

In conclusion, the *Ross* court found that there were genuine issues of material fact about whether the circumstances of the case constituted a direct impact within the Indiana impact rule, and whether the plaintiff's emotional trauma was the reasonable result of such impact.[209] It held that these are both questions of fact to be determined by a jury, and not by the courts as a matter of law.[210]

VI. Medical Malpractice

In *Auler v. Van Natta*,[211] the plaintiff brought a medical malpractice action against her surgeon and the hospital in which she was treated, claiming lack of informed consent for the implantation of a saline breast implant. At the time of her surgery, the plaintiff was suffering from cancer of her left breast. She was admitted to the defendant hospital for removal of the breast and reconstructive surgery.[212] Prior to surgery, the plaintiff informed her surgeon that she did not want a breast implant. She subsequently signed a general consent form, which provided: "The explanation of the operation or special procedure must be given to the patient by the named physician, since only he is competent to do so."[213] Nowhere did the document reflect that a saline breast implant was contemplated.

Following the surgical removal of her breast, the defendant doctor performed the reconstructive surgery, inserting a saline-filled breast implant. "[The plaintiff] was unaware of the implant until the next year when it was observed in a sonogram."[214] The plaintiff subsequently filed a proposed complaint with the Indiana Department of Insurance naming the hospital and surgeon as defendants. "In a unanimous decision, the Medical Review Panel concluded that the [h]ospital had complied with the appropriate standard of care. With regard to the surgeon, the panel found there was a material issue of fact, not requiring expert opinion, concerning the issue of informed consent."[215] The plaintiff then filed a medical malpractice complaint against both the hospital and surgeon. The hospital moved for summary judgment, which was granted by the trial court.[216]

On appeal, the plaintiffs contended that the hospital was liable for

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207. *See id.*
208. *Id.*
209. *Id.*
210. *Id.*
211. 686 N.E.2d 172 (Ind. Ct. App. 1997).
212. *See id.* at 173.
213. *Id.*
214. *Id.*
215. *Id.*
216. *See id.*

malpractice because it failed to obtain her informed consent to the breast implant procedure.[217] She first claimed that the hospital possessed a legal duty, independent from that of the physician, to obtain her informed consent to perform the surgery.[218] As a matter of first impression, the Indiana Court of Appeals concluded that, in the absence of circumstances supporting a claim for vicarious liability or other special circumstances, a hospital has no independent duty to obtain a patient's informed consent.[219] In doing so, the court recognized that:

> [O]ne purpose for securing a patient's informed consent is to protect the patient from a physician who, without a legally sufficient consent, commits a battery. If there is a failure of informed consent, no battery occurs until the surgery or other procedure is performed. However, when the physician performs the procedure in the absence of such consent, it is the physician, not the hospital, who commits the battery.[220]

Thus, the *Auler* court held that because the doctor was not an employee or agent of the hospital, and no other special circumstances were present, the hospital had no independent legal duty to obtain the patient's informed consent.[221]

Alternatively, the plaintiff claimed that by providing the written consent form and obtaining her signature, the hospital had gratuitously assumed the physician's duty to obtain her legal informed consent to the surgery.[222] Recognizing that under Indiana law a party may gratuitously place himself in a position such that the law imposes a duty to perform an undertaking in a manner that will not jeopardize the safety of others,[223] the court analyzed the written consent form signed by the plaintiff. It concluded from the language therein that the hospital's general consent form was not designed to replace the informed consent required to be given by the surgeon, and that the hospital did not undertake to perform the duty of obtaining informed consent.[224] Consequently, the court held that the defendant hospital did not gratuitously assume the physician's duty to obtain informed consent.[225] Absent a duty, the hospital could not be liable for malpractice. Thus, the court affirmed the trial court's entry of summary judgment in favor of the hospital.[226]

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217. *See id.* at 174.
218. *See id.*
219. *Id.* at 175.
220. *Id.*
221. *Id.*
222. *See id.*
223. *Id.* (citing Johnson v. Owens, 639 N.E.2d 1016, 1019 (Ind. Ct. App. 1994)).
224. *Id.* at 176.
225. *Id.*
226. *Id.*

VII. WRONGFUL DEATH

During this survey period, the Indiana Court of Appeals decided several cases addressing who is entitled to recover under Indiana's Wrongful Death Statute.[227] In *Manczunski v. Frye*,[228] the Indiana Court of Appeals held that a fiancé is not entitled to recover under Indiana's Wrongful Death Statute.[229] The plaintiff argued that given "the totality of the circumstances" (i.e., that the couple had lived together for two years, received a marriage license and were to be married in six days), he should be entitled to bring a wrongful death suit for the death of his fiancé. The court found that both the statute and case law precedent were clear and refused to permit the plaintiff's cause of action to proceed by granting defendant's motion for summary judgment.[230]

In *Estate of Miller v. City of Richmond*,[231] the court held that the parents of a twenty-three-year-old were not "dependent next-of-kin" within the statutory definition of Indiana's Wrongful Death Statute.[232] In *Miller*, the decedent was the son of the plaintiffs. He lived at home while he attended a vocational college full time and worked for two family businesses.[233] The decedent and his father each owned one-half of a welding business and the decedent, his father and step-brother owned a supply business.[234] The parents argued that they were dependent next-of-kin because their son partially supported them through his contributions in working for the family businesses.[235]

The trial court granted summary judgment to the plaintiffs on the issue of liability. However, it agreed with the defendants that the plaintiffs were not dependent next-of-kin under Indiana's Wrongful Death Statute and thus granted summary judgment to the City.[236]

The court, quoting *Wolf v. Boren*,[237] stated that the standard for dependency within the meaning of the wrongful death statute requires proof of "'a need or necessity of support on the part of the person alleged to be dependent . . . coupled with the contribution to such support by the deceased.'"[238] The "dependency

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227. IND. CODE § 34-23-1-1 (1998). The court in *Manczunski v. Frye*, 689 N.E.2d 473, 474 (Ind. Ct. App. 1997), cited Indiana Code section 34-1-1-2 (1988), which was repealed and replaced in 1998.

228. 689 N.E.2d 473 (Ind. Ct. App. 1997).

229. *Id.* at 474.

230. *Id.*

231. 691 N.E.2d 1310 (Ind. Ct. App. 1998).

232. *Id.* at 1313.

233. *See id.* at 1311.

234. *See id.*

235. *Id.* at 1312.

236. *See id.* at 1311.

237. 685 N.E.2d 86 (Ind. Ct. App. 1997). *Wolf* was discussed in last year's survey issue of the *Indiana Law Review*. Tammy J. Meyer & Mark E. Walker, *Recent Developments in Indiana Tort Law*, 31 IND. L. REV. 839, 844 (1998).

238. *Estate of Miller*, 691 N.E.2d at 1312 (quoting *Wolf*, 685 N.E.2d at 88)).

must be actual, amounting to a necessitous want on the part of the beneficiary and a recognition of that necessity by the decedent."[239] There must be "an actual dependence coupled with a reasonable expectation of support or with some reasonable claim to support from the decedent."[240]

In its analysis, the court pointed to two federal district court cases that had addressed similar issues. In *Mehler v. Bennett*,[241] the court found that services rendered by the decedent to a corporation were not sufficient to constitute an actual contribution of services for the support of the beneficial claimants; rather, the court held that services inured directly to the corporation and not the parents.[242] The court made a similar finding in *Heinhold v. Bishop Motor Express, Inc.*[243]

The *Miller* court held that the provision of services, for pay, to a business entity, particularly where the decedent was an owner of the business, does not constitute support of dependency even though the party claiming dependency owns a portion of the business.[244] The court appeared to give considerable weight to the fact that the decedent's parents were able-bodied individuals who were employed full time and whose income actually increased after their son's death.[245] The court also noted that it was the son who appeared dependent on the parents, as they had been claiming him as a dependent upon their tax returns.[246]

Within a few weeks of the *Miller* decision, the court of appeals, in a rather unusual case of first impression, addressed the dependent next-of-kin issue in relation to dependant remote relatives when closer non-dependant relatives exist. In *Luider v. Skaggs*,[247] Kammerer was killed in an automobile accident. Luider, Kammerer's second cousin, subsequently brought a wrongful death suit. The defendants moved for summary judgment, arguing that Luider was not a dependent next-of-kin because the decedent was survived by a relative closer in consanguinity, a brother.[248] The trial court agreed with the defendants' argument and granted summary judgment in favor of the defendants without reaching the issue of dependency based on Luider's gainful employment.[249]

The sole issue before the court of appeals was whether Indiana's Wrongful Death Statute permits a decedent's remote dependent relative to maintain a cause of action as a dependent next-of-kin even when there are closer non-dependent relatives in existence.[250] Acknowledging a U.S. Supreme Court case that had

239. *Id.*
240. *Id.*
241. 581 F. Supp. 645 (S.D. Ind. 1984).
242. *Id.* at 648.
243. 660 F. Supp. 382 (N.D. Ind. 1987).
244. *Estate of Miller*, 691 N.E.2d at 1313.
245. *Id.*
246. *Id.*
247. 693 N.E.2d 593 (Ind. Ct. App. 1998).
248. *See id.* at 595.
249. *See id.*
250. *Id.* at 595.

addressed the issue,[251] the court found that "the degree of kinship alone should not be the sole factor in a wrongful death action."[252] Instead, "the issue of dependency should also define the right."[253] The court noted that even though the decedent had a surviving brother who was next in line under Indiana's intestate succession statute, the case was not one of intestate succession but one of alleged dependency.[254]

The *Luider* court reversed the trial court's ruling and remanded the case for a determination of whether Luider was a dependent.[255] It noted several facts showing dependency, including the facts that the parties lived together, owned a ranch, pooled their resources, combined their incomes, paid joint debts, had a "Living Together Agreement," held joint life insurance policies and executed a single will.[256] The court also noted that there was evidence that Luider had experienced financial hardship since Kammerer's death.[257] Of particular interest, the court found that despite the familial lineage, the parties were living together as husband and wife.[258] The court remanded the case for a determination of whether Luider was in fact a dependent next-of-kin based on these facts.[259]

Within a week of the *Luider* decision, the court of appeals was once again faced with the issue of dependent next-of-kin in *Chamberlain v. Parks.* [260] In *Chamberlain*, the decedent's parents brought a wrongful death action against the driver of a vehicle that had struck their son's vehicle. The defendants challenged the parents' standing as dependent next-of-kin. The trial court granted the defendants' motion for summary judgment, finding that the parents were not dependent next-of-kin.[261] The parents appealed and challenged the constitutionality of Indiana's Wrongful Death Statute and the issue of their dependency, alleging that they were entitled to bring a common law wrongful death action.

As to constitutionality, the parents claimed that because both financially dependant and independent parents are emotionally dependant upon their children, there is no reasonable basis to treat dependant parents differently under Indiana's Wrongful Death Statute.[262] The court noted that it must judge the constitutionality challenge to the statute based on the two-prong test set forth in

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251. *See* Poff v. Pennsylvania R.R., 327 U.S. 399 (1946).

252. *Luider*, 693 N.E.2d at 596.

253. *Id.*

254. *Id.*

255. *Id.* at 597.

256. *Id.*

257. *Id.*

258. This appeared to be a factor in the court's analysis although, as noted in *Manczunski v. Frye*, 689 N.E.2d 473, 474 (Ind. Ct. App. 1997), if the parties are not legally married this should not be an issue.

259. *Luider*, 693 N.E.2d at 597.

260. 692 N.E.2d 1380 (Ind. Ct. App. 1998).

261. *See id.* at 1381-82.

262. *See id.* at 1382.

Collins v. Day,[263] which provides:

> First, the disparate treatment accorded by the statute must be reasonably related to inherent characteristics which rationally distinguish the unequally treated classes. Second, the preferential treatment must be uniformly applicable and equally available to all persons similarly situated.[264]

The *Chamberlain* court found that recoverable emotional damages under Indiana's Wrongful Death Statute derive from a dependent-caregiver relationship, not that of a parent-child. It further found that the classification scheme is based upon the party's dependency on the deceased and that the disparate treatment must be rationally related to the parent's dependency.[265] Thus, the court held that limiting damages to those who are dependant satisfies the first prong of the *Collins* test.[266] As to the second prong, the court held that the statute was constitutional because it applied equally to all dependent next-of-kin.[267]

The court next addressed the parents' dependency argument. The parents claimed that although their son did not provide them with financial support, they were dependent upon him for various personal services, such as groceries, house cleaning, yard work, painting and vehicle repair.[268] The court found that although the son occasionally performed services for his parents, he did not contribute to their support in a tangible and material way; rather, his acts were ones of generosity, gifts and donations, as he lived with his parents and received free room and board, automobile insurance and the like.[269]

Finally, the court found that the parents were not entitled to bring an action at common law for wrongful death, as actions for wrongful death are purely statutory.[270]

The dependant next-of-kin issue was addressed again in *Necessary v. Inter-State Towing*.[271] In *Necessary*, Juanita was killed in an automobile accident and was survived by Scott, her adult son, and Joseph, Scott's adult son. The three had resided together and shared household expenses. Juanita made mortgage payments until 1991, and thereafter shared them with Scott.[272] Scott purchased a car for Juanita, and Joseph paid rent to Scott. Juanita made monthly payments

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263. 644 N.E.2d 72 (Ind. 1994).

264. *Id.* at 80.

265. *Chamberlain*, 692 N.E.2d at 1382-83.

266. *Id.* at 1383.

267. *Id.*

268. *See id.* at 1383-84.

269. *Id.* at 1384. Judge Riley dissented on this issue, noting that the issue of dependency was an issue of fact in this case. *Id.* at 1385 (Riley, J., dissenting).

270. *Id.* at 1384.

271. 697 N.E.2d 73 (Ind. Ct. App. 1998).

272. *See id.* at 75.

toward food and utilities. Scott paid for lawn care.[273] Juanita also provided Scott and Joseph with love, affection, guidance and services like cooking, cleaning and tailoring. Scott earned the most income and Juanita earned the least of the three. Juanita did not declare her son or grandson on her tax returns. Scott inherited a portion of Juanita's estate, but Joseph did not.[274]

The defendant filed a motion for partial summary judgment, which the trial court granted, finding that because Juanita had no dependants the recoverable damages were limited to medical, hospital, funeral and burial expenses, and the costs of administration.[275] The estate appealed arguing that dependency damages should have been allowed.[276]

Noting that partial dependency is sufficient to establish "necessitous want," the *Necessary* court found that material questions of fact existed regarding the dependency claims that precluded the entry of summary judgment.[277] The court distinguished *Miller*,[278] finding that in *Miller*, the decedent made no financial contributions to his parents, made only occasional contributions of services, and was claimed as a dependent on his parents' tax returns. Further, the primary loss claimed by the parents in *Miller* was the expectation that the son would take over the family business.[279] In *Necessary*, however, Juanita made regular, significant and continuous financial and non-financial contributions on a daily basis.[280]

Next, the court found that assuming dependency, Scott, but not Joseph, would be the sole dependent next-of-kin. The *Necessary* court held that Scott's dependency precluded Joseph from bringing his own dependency claim.[281] Noting its previous decision in *Ludier*,[282] the court found that two conditions must be met for recovery under Indiana's Wrongful Death Statute: dependency *and* heirship.[283]

During this survey period, the Indiana Court of Appeals went to great lengths to clarify the language of Indiana's Wrongful Death Statute. Its decisions reflect a strict interpretation of the language expressed by the legislature as to who is entitled to recover under the statute. Nevertheless, as the number of wrongful death actions brought in the State of Indiana continues to increase, our courts will no doubt face similar issues time and again.

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273. *See id.*
274. *See id.*
275. *See id.*
276. *See id.*
277. *Id.* at 77-78.
278. Estate of Miller v. City of Richmond, 691 N.E.2d 1310 (Ind. Ct. App. 1998).
279. *Id.* at 1313.
280. *Necessary*, 697 N.E.2d at 78.
281. *Id.*
282. Ludier v. Skaggs, 693 N.E.2d 593 (Ind. Ct. App. 1998).
283. *Necessary*, 697 N.E.2d at 80.

VIII. Governmental Entities and the Indiana Tort Claims Act

In *Saunders v. County of Steuben*,[284] the Indiana Supreme Court held, in a case of first impression, that a decedent's act of suicide cannot be the basis for a finding of contributory negligence or incurred risk that would bar a plaintiff's claim for wrongful death of an inmate.[285] The court noted that a custodian has a legal duty to take reasonable steps to protect a person in custody from harm.[286] However, the custodian is not under a duty to prevent a particular act such as suicide because the custodian is not an insurer against harm.[287]

The court found that the degree of notice that a person is a suicide risk is a critical factor in assessing the reasonableness of the steps taken.[288] The focus is on the defendant's conduct under the circumstances, and the plaintiff's actions are only relevant insofar as they are part of those circumstances.[289] To hold that the suicide of a plaintiff barred a claim against a governmental entity based on comparative fault or incurred risk would obviate the custodian's legal duty to protect the plaintiff from that very form of harm.[290]

Chief Justice Shepard dissented from the majority opinion, stating that the statements that a custodian does not have a duty to prevent a particular act such as suicide but does have a duty to take reasonable steps to protect life (including self-harm) are inconsistent.[291] Chief Justice Shepard noted that the majority decision, in effect, holds that while custodians have a duty to prevent self-harm, detainees have no duty at all to care for themselves.[292] He further noted that other non-governmental custodians like hospitals, psychiatric centers and juvenile homes, will be adversely affected and will find themselves insurers of the safety of those in their care.[293] Chief Justice Shepard did not address the fact that non-governmental entities can raise the defense of comparative fault and reduce an award to a plaintiff based on the plaintiff's fault. However, in *Saunders*, this would preclude recovery by the plaintiff; the very circumstance the court appears to be trying to avoid.

In another case of first impression, the Indiana Supreme Court, in *Budden v. Board of School Commissioners of Indianapolis*,[294] held that a tort claims "notice by a putative class representative that fairly signals an intent to assert a class claim, but does not list all potential plaintiffs, compl[ies] with the notice

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284. 693 N.E.2d 16 (Ind. 1998).
285. *Id.* at 17.
286. *Id.* at 18.
287. *See id.*
288. *Id.* at 19.
289. *See id.*
290. *See id.*
291. *Id.* at 22 (Shepard, C.J., dissenting).
292. *Id.*
293. *Id.* at 23.
294. 698 N.E.2d 1157 (Ind. 1998).

requirement to preserve claims of class members'[295] who subsequently seek class certification under Trial Rule 23.

In analyzing this issue, the court first found that the plaintiffs' notice satisfied the language of the Indiana Tort Claims Act ("ITCA"),[296] reasoning that the ITCA merely requires notice from the person making the claim and that those terms are not defined.[297] Accordingly, the court held that there was nothing in the ITCA to suggest that "the claim" cannot be a class action or that unknown class members must be identified by name; other "persons involved" must be identified if known.[298] The purpose of the ITCA is to provide notice to the political subdivision, not to create barriers to claims.[299]

In *Greater Hammond Community Service v. Mutka*,[300] the Indiana Court of Appeals addressed whether a not-for-profit corporation was a governmental instrumentality entitled to the protection of the liability cap of the ITCA.

A group of Hammond residents founded and incorporated Hammond Opportunity Center, Inc. as a not-for-profit corporation. The name was later changed to Greater Hammond Community Services, Inc. ("GHCS"). GHCS entered into a contract with Lake County Equal Opportunity Council, Inc. ("LCEOC"), a community action agency under the ITCA, to provide services to low income, elderly and physically impaired Hammond residents. This included providing transportation for the elderly.[301]

Mutka was a passenger on a bus driven by King, an employee of GHCS, when the bus collided with another car. As a result of the collision, Mutka was injured. LCEOC leased the bus from the Northern Indiana Regional Planning Commission ("NIRPC"). Mutka sued LCEOC, GHCS, NIRPC and King.[302] The parties stipulated that LCEOC and NIRPC were governed by the ITCA. The defendants filed a motion for summary judgment seeking a declaration that all defendants were governed by the ITCA and that the aggregate liability of the defendants could not exceed the liability cap of $300,000 pursuant to the act.[303] GHCS argued that it was a political subdivision or, alternatively, that it was a division of LCEOC and entitled to the protection of the liability cap.[304] Mutka cross moved for summary judgment, arguing that the cap did not apply to GHCS because it was not a community action agency or other governmental entity. The trial court granted Mutka's motion and held that the ITCA did not apply to GHCS.[305]

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295. *Id.* at 1158.
296. IND. CODE §§ 34-13-3-1 to -25 (1998).
297. *Budden*, 698 N.E.2d at 1161-62. *See also* IND. CODE § 34-13-3-10 (1998).
298. *Budden*, 698 N.E.2d at 1162.
299. *See id.* at 1163.
300. 699 N.E.2d 757, 758 (Ind. Ct. App. 1998).
301. *See id.*
302. *See id.*
303. *See id.* at 758-59.
304. *See id.* at 759.
305. *See id.*

GHCS appealed, arguing that despite the fact that it was not a community action agency as defined by Indiana Code section 12-14-23-2, as a private not-for-profit corporation providing essential government services it was an instrumentality of the state entitled to the protections of the ITCA.[306] GHCS relied upon the Indiana Supreme Court decision in *Ayres v. Indiana Heights Volunteer Fire Department*,[307] in support of its argument.[308]

In *Ayres*, the Indiana Supreme Court held that a volunteer fire department was entitled to the immunity afforded by the ITCA because firefighting was a service uniquely governmental and private enterprises are not in the business of fighting fires.[309] The *Ayres* court held that the volunteer fire department was an instrumentality of the local government and protected by the ITCA.[310]

In *Mutka*, the Indiana Court of Appeals distinguished *Ayres*, finding that GHCS was not a statutory creation but a private not-for-profit group of Hammond residents independent of any governmental entity.[311] Additionally, unlike the volunteer fire department, GHCS did not offer a service uniquely governmental.[312] Thus, the court affirmed the trial court's ruling that GHCS was not entitled to the statutory cap provided in the act.[313]

However, a contrary result was reached in *LCEOC, Inc. v. Greer*,[314] where the Indiana Court of Appeals held that LCEOC was a community action agency and thus a political subdivision under the ITCA and that GHCS was also a political subdivision within the meaning of the ITCA.[315] The court found that because GHCS was a provider of services governmental in nature and because it was administered by LCEOC, it was a governmental entity entitled to the protections of the ITCA.[316]

Interestingly, the *Mutka* and *Greer* decisions were rendered on the same date. The *Mutka* decision was written by Judge Darden with Judges Garrard and Staton concurring.[317] *Greer* was written by Judge Riley with Judges Bailey and Najam concurring.[318]

306. *See id.* at 760.
307. 493 N.E.2d 1229 (Ind. 1986).
308. *See Mutka*, 699 N.E.2d at 760.
309. *Ayres*, 493 N.E.2d at 1235.
310. *Id.* at 1237.
311. *Mutka*, 699 N.E.2d at 760.
312. *See id.*
313. *Id.*
314. 699 N.E.2d 763 (Ind. Ct. App. 1998).
315. *Id.* at 767, 769.
316. *Id.* at 769.
317. *Mutka*, 699 N.E.2d at 758, 762.
318. *Greer*, 699 N.E.2d at 764, 769.

IX. Abuse of Process

In *National City Bank, Indiana v. Shortridge*,[319] the Indiana Supreme Court held that attorneys representing a personal injury plaintiff could not escape a defendant's claim of abuse of process by way of summary judgment.[320] The plaintiff's attorneys had filed a *lis pendens* notice against certain real estate owned by the defendants. The trial court ruled that the *lis pendens* was improper and ordered it removed.[321] Despite this ruling, the attorneys filed a second *lis pendens* notice, which caused the sale of the property to collapse. The Indiana Supreme Court held that issues of fact precluded summary judgment.[322]

Despite the trial court and court of appeals' findings that the attorney's actions were within a range of legitimate ends and justifiable conduct precluding the abuse of process claim, the Indiana Supreme Court held to the contrary.[323] The court noted that because the use of *lis pendens* was so plainly wrong and because the attorneys did not have a proper justification for filing the second *lis pendens*, the inference that the attorneys may have made improper use of the legal process existed.[324]

National City appears to open the door (at least a crack) for claims against attorneys for abuse of process. Only as future claims are filed will the impact of the Indiana Supreme Court's decision truly come to light.

X. Invasion of Privacy

The specter of AIDS entered the legal realm once again in *Doe v. Methodist Hospital*,[325] where the Indiana Supreme Court declined to recognize the tort of invasion of privacy when private facts are publically disclosed, at least on the facts as presented in *Doe*. The plurality opinion addressed the issue as one of first impression in the State of Indiana.[326]

In *Doe*, the plaintiff, a letter carrier for the U.S. Postal Service, was rushed by ambulance from work to the hospital due to a suspected heart attack. Doe informed the paramedics that he was HIV positive.[327] He had previously disclosed this to a small circle of close friends and co-workers, but not to his co-workers generally. While in the hospital, Cameron, a co-worker, checked on Doe's condition by calling his own wife who worked at the hospital. She disclosed that Doe was HIV positive and Cameron told some of Doe's co-

319. 689 N.E.2d 1248 (Ind. 1997).

320. *Id.* at 1249.

321. *See id.* at 1250.

322. *Id.* at 1253.

323. *Id.*

324. *Id.*

325. 690 N.E.2d 681, 682 (Ind. 1997).

326. The concurring opinion noted that this was not a case of first impression in Indiana. *Id.* at 694 (Dickson, Sullivan, JJ., concurring with separate opinion).

327. *Id.* at 683.

workers, including Duncan.[328] Duncan told Saunders and Okes the news. Saunders was not aware of Doe's condition, but Okes, a close friend of Doe's, was aware. Doe subsequently sued Duncan for invasion of privacy.[329]

The trial court granted Duncan's motion for summary judgment and the court of appeals affirmed. The Indiana Supreme Court granted transfer and also affirmed.[330]

The supreme court went through a lengthy discussion of the genesis of the tort of invasion of privacy, initially noting that it originated from a 1890 law review article written by a Boston attorney, Samuel Warren. Apparently, the press had been covering Warren's wife's social gatherings "in highly personal and embarrassing detail."[331] Thereafter, a few courts rejected the new tort,[332] while at least one accepted it.[333]

The First Restatement of Torts articulates a two dimensional interest in "'not having [one's] affairs known to others or [one's] likeness exhibited to the public.'"[334] By 1960, Professor Prosser had concluded that invasion of privacy consisted of four separate and independent torts.[335] The Second Restatement adopted his view and described the four injuries as follows: "(1) intrusion upon seclusion; (2) appropriation of likeness; (3) public disclosure of private facts; and (4) false-light publicity."[336]

The "subpart" of the tort of invasion of privacy at issue in *Doe* was the disclosure of private facts. The court noted that this cause of action was recognized in most states, but that Indiana had never directly confronted the issue.[337]

The court identified two main interests that the duty to refrain from publically disclosing private affairs of others would protect: reputation and mental well-being. It noted that these interests must be balanced against competing public and private interests.[338] Addressing the issue of reputation, the court found that "[t]ruthful disclosures can be socially disruptive and personally dangerous."[339] It further found that under defamation law in Indiana, truthful but

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328. *See id.*

329. *Id.* at 683. Doe also sued the hospital and Cameron for invasion of privacy and for violating statutory duties of confidentiality. Those issues were not presented in the appeal. *Id.*

330. *Id.* at 684.

331. *Id.* (citing William L. Prosser, Privacy, 48 CAL. L. REV. 383 (1960)).

332. *See id.*; *see also* Atkinson v. John E. Doherty & Co., 80 N.W. 285 (1899); Roberson v. Rochester Folding Box Co., 64 N.E. 442 (N.Y. 1902).

333. *See Doe*, 690 N.E.2d at 684; *see also* Pavesich v. New England Life Ins. Co., 50 S.E. 68 (1905).

334. *Doe*, 690 N.E.2d at 684 (quoting RESTATEMENT OF TORTS § 867 (1938)).

335. *See id.* (citing Prosser, *supra* note 331, at 389).

336. *Id.* (citing RESTATEMENT (SECOND) OF TORTS § 652A (1977)).

337. *Id.* at 685.

338. *Id.* at 686.

339. *Id.*

defamatory statements have not been civilly actionable.[340] Citing a potential conflict with the Indiana Bill of Rights (in which truth is a justification in prosecution for libel), the court found that caution should be exercised in recognizing a civil cause of action for truthful defamation.[341]

The court then addressed the interest of emotional health. It initially pointed out that Indiana already provides a remedy for one injured emotionally by another through the tort of intentional infliction of emotional distress, otherwise known as "outrage."[342] However, under the tort of outrage, a plaintiff must prove a mental element that is not required under the public disclosure tort. The latter is a strict liability version of outrage, or "outrage lite."[343]

The key elements for the tort of public disclosure of private facts are: a "person (1) gives 'publicity;' (2) to a matter that (a) concerns the 'private life' of another; (b) would be 'highly offensive' to a reasonable person; and (c) is not of legitimate public concern."[344]

In *Doe*, Duncan argued that Doe's claim failed with regard to Okes because of the "private life" element, and failed with regard to Saunders because of the "publicity" element. The Indiana Supreme Court agreed on both counts.[345] As to Okes, Doe had already told Okes of his HIV status.[346] As to Saunders, there was no dissemination to the general public.[347] The court held that "'publicity' requires communication of the information 'to the public at large, or to so many persons that the matter is regarded as substantially certain to become one of public knowledge.'"[348] Communication to a single person or small group of persons is not actionable. Although not adopting a looser standard, the court noted that some courts have held that the publicity element is satisfied if the publicity is to a particular public or person who has a special relationship with the plaintiff (such as a spouse).[349] Even under such a broad definition of publicity, the court held that, Duncan's disclosure to Saunders did not amount to publicity because there was no special relationship.[350] There was no evidence that the disclosure to Saunders was any more damaging than to the other letter carriers Doe had told.[351] In so holding, the court concluded that the facts of *Doe* did not persuade it to endorse the subtort of disclosure.[352]

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340. *Id.* at 687.

341. *Id.* at 691. The concurring opinion did not agree that there was any conflict. *Id.* at 695 (Dickson, Sullivan, JJ., concurring with separate opinion).

342. *Id.* at 691.

343. *Id.*

344. *Id.* at 692 (citing RESTATEMENT (SECOND) OF TORTS § 652D (1977)).

345. *Id.*

346. *See id.* at 692 n.15.

347. *See id.* at 692.

348. *Id.* (quoting RESTATEMENT (SECOND) OF TORTS § 652D cmt. a (1977)).

349. *Id.* at 693.

350. *Id.*

351. *See id.*

352. *Id.* at 695.

TRUSTS AND DECEDENTS' ESTATES

CYNTHIA ADAMS*

Some interesting developments took place in the areas of trusts and estates during this survey period. The most notable decisions and legislation are discussed in the following sections, covering decedents' estates, inheritance tax, trusts, powers of appointment, and guardianships.

I. DECEDENTS' ESTATES

A. *Constructive Trust Arising from Murder of Decedent*

In *Heinzman v. Mason*,[1] the court addressed the issue of whether a constructive trust should be imposed to prevent a husband's children from a previous marriage from inheriting the wife's property when the husband committed suicide immediately after taking the wife's life. The morning after being served with a restraining order and an order to appear in connection with a petition for dissolution of marriage filed by the wife, the husband went to the wife's workplace, shot and killed her, then shot and killed himself. Both the husband and wife died intestate.[2] The couple, married since 1982, had no children born of the marriage, but the husband had four adult children from a prior marriage. The wife had acted as a mother to these children, but had not adopted them. The wife's heirs at law were determined to be her aunts, uncles, and their issue, while the husband's heirs were his four adult children by a previous marriage.[3]

The administrator of the husband's estate filed a petition to set aside the determination of heirship in the wife's estate. She also moved for summary judgment, claiming: 1) under Indiana Code section 29-1-2-1(b)(3),[4] the wife's property passed to the husband as the surviving spouse; 2) Indiana Code section 29-1-2-12.1[5] did not apply because the husband was not convicted of a crime in

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* Lecturer in Law, Indiana University School of Law—Indianapolis. B.A., Kentucky Wesleyan College; J.D., Indiana University.

1. 694 N.E.2d 1164 (Ind. Ct. App. 1998).
2. *See id.* at 1166.
3. *See id.*
4. IND. CODE § 29-1-2-1(b)(3) (1998).
5. *Id.* § 29-1-2-12.1. This section provides, in pertinent part:

> (a) A person is a constructive trustee of any property that is acquired by him or that he is otherwise entitled to receive as a result of a decedent's death, if that person has been found guilty, or guilty but mentally ill, of murder, causing suicide, or voluntary manslaughter, because of the decedent's death. A judgment of conviction is conclusive in a subsequent civil action to have the person declared a constructive trustee.
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> * * *
>
> (c) If a constructive trust is established under this section, the property that is subject to the trust may be used only to benefit those persons, other than the constructive trustee, legally entitled to the property, determined as if the constructive trustee had died immediately before the decedent. However, if any property that the constructive trustee

connection with his wife's death as mandated by that statute and that no other statute prevented the husband from inheriting his wife's estate; and 3) no equitable reason prevented the husband's children from receiving the wife's property.[6] Nevertheless, the court of appeals affirmed the trial court's judgment to impose a constructive trust on the wife's property in the husband's estate for the benefit of her heirs.[7]

The court conceded that Indiana Code section 29-1-2-12.1 was not applicable to the case because the husband was not charged with any crime for causing the wife's death.[8] It also conceded that there was no other applicable statute that mandated the creation of a constructive trust under the facts of this case.[9] But, despite the absence of statutory authority, the court concluded that established principles of equity supported its conclusion that it had the power to impose a constructive trust upon any property acquired by a wrongdoer or his estate when the wrongdoer kills his spouse and then commits suicide before he can be charged or convicted of causing the death.[10]

Specifically, the equitable principle that neither the one who feloniously kills his spouse nor his heirs should benefit from the killer's wrongdoing prevented

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> acquired as a result of the decedent's death has been sold to an innocent purchaser for value who acted in good faith, that property is no longer subject to the constructive trust, but the property received from the purchaser under the transaction becomes subject to the constructive trust.

Id.

6. *See Heinzman*, 694 N.E.2d at 1166.

7. *Id.* at 1167-68. The court of appeals affirmed the trial court's grant of summary judgment in favor of the administrator of the wife's estate. *Id.* at 1168. The court stated with approval the trial court's finding that the proceeds from the wife's life insurance policy and the wife's bank accounts went to the husband as sole named beneficiary of the insurance policy and accounts, and then into his estate upon his death. *Id.* at 1166. Also, the wife's other property did pass to the husband as provided under Indiana Code section 29-1-2-1(b)(3), and then into his estate upon his death. *See id.* Finally, because it was the husband's wrongdoing that resulted in his wife's death, the trial court appropriately concluded that all of the wife's property, including the proceeds from the wife's life insurance policy, was subject to a constructive trust for the benefit of the wife's heirs. *See id.* (citing National City Bank of Evansville v. Bledsoe, 144 N.E.2d 710 (Ind. 1957); New York Life Ins. Co. v. Henriksen, 415 N.E.2d 146 (Ind. Ct. App. 1981); Stacker v. Mack, 130 N.E.2d 484 (Ind. App. 1955)).

8. *Id.* at 1167.

9. *Id.*

10. *Id.* (citing *Bledsoe*, 144 N.E.2d at 710). In *Bledsoe*, the Indiana Supreme Court imposed a constructive trust on one-half of the property held by the spouse and his deceased wife as tenants by the entireties when the spouse killed his wife then killed himself before he could be convicted, although no statute addressed such a situation. *Bledsoe*, 144 N.E.2d at 715. In support of its holding, the court stated that Indiana Code section 29-1-2-12 (providing for the imposition of a constructive trust when one was convicted of causing the death of the decedent), which was the predecessor of the current Indiana Code section 29-1-2-12.1, was "not intended to supersede but merely to supplement the prevailing equity rule . . . ." *Id.*

the children in this case from inheriting the wife's property, even though they were not involved in any misconduct leading to her death.[11] Further, to allow the children to inherit would still confer a benefit upon the husband for his wrongdoing.[12] Almost as an afterthought, the court added that it could not overlook the possibility that the husband may have intended to benefit his heirs when he took his wife's life and then took his own.[13] Speculation as to the husband's intent seems unnecessary. The husband, by his wrongdoing, seized control of his wife's property, thereby denying her the right to dispose of her property as she saw fit.[14] Although his suicide prevented any lifetime transfer of her property, certainly he still retained control of her property by his death transfer.

B. Spouse's Statutory Election to Take Against the Will

The court in *Dunnewind v. Cook*,[15] held that assets in an inter vivos trust are subject to a surviving spouse's statutory right to an elective share of the deceased spouse's estate[16] when the decedent had created the trust in contemplation of her own imminent death and with the purpose of defeating the surviving spouse's statutory elective share.[17] The decedent was survived by her spouse from a second marriage and her two children born of a prior marriage. No children were born of the second marriage. Upon her death in 1995, decedent left a will, executed in 1976, more than three years after her marriage to the surviving spouse, and a irrevocable inter vivos trust, created only a few months prior to her death.[18]

The decedent's will devised all of her solely owned property to her two children and made no provision for her surviving spouse. The decedent did not change her will or seek estate planning advice until early 1995, a few months after she was diagnosed with terminal cancer.[19] The decedent's daughter, who had arranged the decedent's meeting with the attorney, later testified that the decedent had stated that she wanted her children to receive her property. Following the attorney's advice, the decedent executed an irrevocable inter vivos

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11. *See Heinzman*, 694 N.E.2d at 1167.

12. *See id.*

13. *Id.* at 1167-68 (citing *In re* Estate of Cox, 380 P.2d 584 (Mont. 1963)).

14. *Accord Bledsoe*, 144 N.E.2d at 714. Although *Bledsoe* addressed the control of property held as tenants by the entireties, the same rationale used by the court in that case to support imposing a constructive trust could be applied here. The *Bledsoe* court reasoned: "There is no doubt the murderer in reality has profited from illegally causing the death of the victim spouse, as he has become the sole and exclusive owner of the fee, which he could thereupon alienate or dispose of as he alone saw fit." *Id.*

15. 697 N.E.2d 485 (Ind. Ct. App. 1998).

16. *See* IND. CODE § 29-1-3-11 (1998).

17. *Dunnewind*, 697 N.E.2d at 490.

18. *See id.* at 487.

19. *See id.*

trust. The trust provisions gave the decedent's spouse a life estate in the marital residence and a life estate in the household goods and personal property used in the marital residence.[20] It also provided that upon the decedent's death the surviving spouse would receive $24,500.[21] Although the surviving spouse was aware of the trust, he never inquired about the trust provisions and was not informed of the provisions. The decedent's children were named as the trust's remainder beneficiaries. Interestingly, the trust did not make any provisions for the decedent during her lifetime, and the trial court found no evidence that the trust was created to assist the decedent in the management of her affairs.[22] Yet, despite the failure of the trust to provide for the decedent, the decedent's daughter continued to pay all the trust's income to the decedent until the decedent's death a few months later.[23]

After the decedent's death, the surviving spouse petitioned the court to determine the assets of the estate and to set aside the trust. The trial court held, and the court of appeals agreed, that the assets remaining in the trust at the decedent's death were subject to the surviving spouse's election because the trust's only purpose was to avoid the statutory election of the surviving spouse.[24]

Relying on *Walker v. Lawson*[25] and *Crawfordsville Trust Co. v.*

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20. *See id.*

21. *See id.* Pursuant to Indiana Code section 29-1-3-1(a), the surviving spouse in *Dunnewind* would be entitled to take one-third of the decedent-spouse's net personal estate plus a life estate in one-third of the decedent-spouse's real estate because he was a subsequent spouse who did not have children by the decedent-spouse and the decedent-spouse left surviving children who were born of a previous marriage. IND. CODE § 29-1-3-1(a) (1998). Presumably, by electing to take his statutory elective share, the spouse in *Dunnewind* stood to receive more than what was provided in the trust.

22. *See Dunnewind*, 697 N.E.2d at 488. The trust provisions and the circumstances surrounding the creation of this trust can easily be distinguished from the inter vivos trust in *Leazenby v. Clinton County Bank & Trust Co.*, 355 N.E.2d 861 (Ind. App. 1976) (holding that a valid inter vivos trust defeated the surviving spouse's statutory election to take against the will). *See infra* note 25 (discussing the Indiana Supreme Court's efforts in *Walker v. Lawson*, 526 N.E.2d 968 (Ind. 1988), to distinguish the inter vivos trust in *Leazenby* from property transfers in contemplation of death that are made in an attempt to deprive the spouse of a share in the property).

23. *Dunnewind*, 697 N.E.2d at 488.

24. *Id.* at 490.

25. 526 N.E.2d 968 (Ind. 1988). In *Walker*, the court held that an attorney was not negligent for his failure to advise a testatrix that her spouse could make a statutory election to take against the will when the testatrix sought the attorney's advice regarding how to dispose of her estate in contemplation of her impending death. *Id.* at 969-70. The *Walker* testatrix approached the attorney for estate planning advice shortly after discovering she had cancer. She mentioned to the attorney that she desired her two children receive her entire estate. In response, the attorney prepared a will that provided that the entire estate would pass in trust for the benefit of the testatrix's children. *See id.* at 969. The will specifically acknowledged that the spouse was purposely omitted from receiving her estate because he benefitted from residing in the residence during the testatrix's lifetime and would continue to reside there as the guardian of the testatrix's children. The *Walker*

Ramsey,[26] the court noted that Indiana law will not permit a gift to withstand a spouse's statutory election to take against the will when it is a *gift causa mortis* or testamentary in effect.[27] Employing an intent test that considers such factors as the settlor's motive in creating such a trust and the timing of the creation of the trust, the court found that the irrevocable inter vivos trust in *Dunnewind* was testamentary in effect.[28] The case facts strongly support this finding. First, the decedent had sought estate planning advice from an attorney only after discovering that she was terminally ill and death was imminent.[29] Second, the decedent had made the statement that she wanted to ensure her children received her property. This statement, combined with the fact that she followed the attorney's advice to create a trust instead of amending her will, showed that she intended to defeat her spouse's share.[30] Third, the trust was testamentary in nature because it failed to provide the decedent with income or the right to reside in her own home, which, in turn, implied that the "gifts"—the res of the trust—were not to take effect until the decedent's death.[31]

C. *Will Contests*

The issues presented in *Fitch v. Maesch*[32] arose from the question of whether a will's execution properly complied with statutory requirements.[33] Here, the

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court also rejected the claim that the attorney could have prevented the surviving spouse from exercising his statutory right to an elective share by utilizing another method to dispose of the estate, such as creating a trust similar to the trust in *Leazenby*, 355 N.E.2d at 861, or a joint tenancy between the testatrix and her children. In so finding, the court relied on *Crawfordsville Trust Co. v. Ramsey*, 100 N.E. 1049 (Ind. App. 1913), which advanced "the established law that a spouse cannot by gifts in contemplation of death deprive a surviving spouse of his or her statutory share in the estate." *Walker*, 526 N.E.2d at 969. It is important to point out that the *Walker* court distinguished the trust in *Leazenby* by observing that the settlor in *Leazenby* had established the trust for the purpose of obtaining assistance in handling her personal affairs and, as time passed, the trust res was actually used to pay for the settlor's nursing home care. *Id.* Also, the *Walker* court noted that the surviving spouse in *Leazenby* presumably knew of the trust and consented to it, and there was no evidence that the settlor's intent in creating the trust was to frustrate her husband's right to a statutory share in her estate. *Id.*

26. 100 N.E.2d 1049 (Ind. App. 1913) (finding stocks and bonds were subject to a surviving spouse's statutory election and were treated as *gift causa mortis*, rather than a valid inter vivos gift, when the donor assigned the stocks and bonds in anticipation of his death and in an attempt to defraud his spouse).

27. *Dunnewind*, 697 N.E.2d at 489.

28. *Id.* at 490.

29. *See id.*

30. *See id.*

31. *See id. See also supra* note 25 (discussing the distinguishing features of the valid inter vivos trust in *Leazenby*.)

32. 690 N.E.2d 350 (Ind. Ct. App. 1998).

33. *See* IND. CODE § 29-1-5-3(a)(1998). That section provides, in pertinent part:

court of appeals held that evidence of the attorney's habit and routine in supervising the execution of his client's wills could be considered when determining the events surrounding the execution of a will.[34] Also, a witness's testimony regarding the execution of the will, to the extent it conflicts with the events set forth in the will's attestation clause, presents a question of fact for the jury.[35]

The will at issue in *Fitch* contained an attestation clause recounting the events surrounding the execution of the will,[36] which if true, would satisfy the statutory execution requirements.[37] Nonetheless, the court, faced with a deceased witness, the attorney who prepared the will and oversaw its execution, and the only surviving witness offering testimony that conflicted with the events described in the attestation clause, had to determine whether the statutory

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> The execution of a will . . . must be by the signature of the testator and of at least two (2) witnesses as follows:
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> (1) The testator, in the presence of two (2) or more attesting witnesses, shall signify to them that the instrument is the testator's will and . . .
>
> (A) sign the will;
>
> * * *
>
> (2) The attesting witnesses must sign in the presence of the testator and each other.

Id.

34. *Fitch*, 690 N.E.2d at 353.

35. *See id.* at 354 (citing Munster v. Marcrum, 393 N.E.2d 256, 258 (Ind. App. 1979)).

36. The attestation clause in the will stated:

> The above and foregoing instrument, consisting of three (3) typewritten pages, was signed, sealed, published and declared by the said [testatrix] as and for her last will and testament, in the presence of us who, at her request and in her presence and in the presence of each other, have hereunto set our names as subscribing witnesses to the due execution of this will. . . .

Id.

37. The will did not include a self-proving affidavit, which was available under Indiana Code section 29-1-5-3(b) & (c) (Supp. 1983) in effect at the time of the will's execution. Pursuant to Indiana Code § 29-1-7-13(c) (1998), a self-proved will eliminates the need for the witnesses to testify upon filing the will to prove its authenticity, *see* IND. CODE § 29-1-7-9 (1998), by creating a rebuttable presumption of compliance with statutory signature requirements and other execution requirements, unless there is proof of fraud or forgery affecting the self-proving affidavit.

Even so, it should be noted that "[t]he leading rule even prior to the self-proved statute was that the attachment of an attesting clause created a presumption of proper execution of will. [*See, e.g.*, Gardner v. Balboni, 588 A.2d 634 (Conn. 1991); *In re* Estate of Smith, 668 N.E.2d 102 (Ill. App. Ct. 1996).] It is presumed that [Indiana Code section] 29-1-7-13(c) carries an even stronger presumption if there is a self-proving clause." 2A JOHN S. GRIMES, HENRY'S PROBATE LAW & PRACTICE OF THE STATE OF INDIANA 653 (7th ed. 1979).

And see *Gardner*, 588 A.2d at 634, for an exhaustive discussion and survey of the law regarding the evidentiary value of an attestation clause to show compliance with the statutory formalities for executing a will.

execution requirements were actually satisfied.

The court of appeals found that the trial court properly admitted the testimony of the attorney's secretary regarding the attorney's habit and routine practice in supervising the execution of his clients' wills.[38] The court looked to Rule 406 of the Indiana Rules of Evidence,[39] for support in allowing this testimony into evidence. At trial, the secretary testified that, based on sixteen years in the employ of the attorney and witnessing more than 500 wills when the attorney's supervised the will execution, she was aware of the attorney's habit and routine practice.[40] She recounted the attorney's specific routine in supervising the execution of clients' wills, which comported with the events recited in the attestation clause, and that the attorney habitually placed the executed will in a sealed envelope. She also identified the sealed envelope containing the testatrix's will as that of the attorney's law firm and the signature appearing on the envelope as that of the attorney.[41] The *Fitch* court rejected the complainant's argument that the secretary's testimony was irrelevant and inadmissible because it did not concern the attorney's habit under the distinct circumstances of the case at bar.[42] Criticizing the complainant for placing "too fine a point on the matter," the court stated: "The supervision of the execution of wills is the conduct in question and the evidence is relevant to prove how [the attorney] supervised the execution of [the testatrix's] will."[43] Here, the secretary's testimony served not only to establish that the attorney's routine for executing a will was the same as those recounted in the attestation clause, but also to authenticate the attorney's signature as an attesting witness.[44]

After determining the secretary's testimony was admissible, the court moved to the second issue of whether the probate of the will could be supported when the surviving attesting witness did not remember specific aspects of the will's execution. While acknowledging that the witness's testimony raised questions as to what actually occurred during the execution of the testatrix's will,[45] the

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38. *Fitch*, 690 N.E.2d at 353.

39. Indiana Rule of Evidence 406 states, in pertinent part: "Evidence of the habit of a person . . . whether corroborated or not and regardless of the presence of eyewitnesses, is relevant to prove that the conduct of the person . . . on a particular occasion was in conformity with the habit or routine practice." IND. R. EVID. 406.

40. *See Fitch*, 690 N.E.2d at 353.

41. *See id.*

42. *Id.* Apparently, the complainant attempted to draw a distinction between the attorney's habit in supervising will executions when his wife and/or secretary served as an attesting witness and the attorney's habit in such situations when other individuals served as attesting witnesses, as was the case in *Fitch*.

43. *Id.*

44. *See id.*

45. *Id.* at 354. The surviving witness did authenticate her signatures found on the will, one of which appeared at the end of the attestation clause, and even recalled that the purpose of the document was to provide the testatrix's brother with a portion of the testatrix's assets. *See id.* However, her testimony conflicted with the attestation clause inasmuch as she could not recall if

Fitch court pointed to the established rule that "where testimony of the attesting witnesses contradicts the substance of the attestation clause from the will, the conflict presents a question of fact for the jury."[46] The trial court's findings that the will's execution complied with statutory formalities and the witness's testimony was unpersuasive were adequately supported by the will's attestation clause, the envelope containing the will that had been signed by the attorney, and the secretary's testimony as to the attorney's habit and routine in supervising the execution of his client's wills.[47] Therefore, because the will was properly executed and authenticated, the court held that it was properly admitted to probate.[48]

D. Determination of Heirship

Estate of Lamey v. Lamey,[49] addressed the issue of whether a decedent's brother had standing to petition the court for an order requiring the decedent's former wife and daughter to submit to blood testing to ascertain whether the daughter was the biological child of the decedent and thus was the heir of the estate. With one exception not disputed in this case, Indiana law looks to the time of death to determine the heirs of the estate.[50] Decedent died intestate without a spouse. The daughter, presumed to be his issue because she was born during the marriage of the decedent and his former wife,[51] was his only surviving child and thus heir to his entire estate.[52]

The uncle attempted to challenge the child's right to inherit the decedent's estate by crafting an argument that Indiana Code section 29-1-2-7 provided him with an avenue to request paternity blood testing so long as the request was made

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anyone other than the testatrix was in the room when she signed the will as a witness or whether she or anyone else was present when the testatrix signed the will. *See id.* Also, she testified that she had not been aware that the document was a will. *See id.*

46. *Id.* (citing Munster v. Marcrum, 393 N.E.2d 256, 258 (Ind. App. 1979) (holding that where the testimony of two attesting witnesses contradicted the events set forth in the attestation clause it presented a question of fact for the jury, and on appeal, the court refused to disturb the finding of the jury that the witnesses' testimony was unpersuasive when the evidence and inferences presented at trial did not lead to a conclusion opposite that reached by the jury).

47. *See id.*

48. *Id.* at 355.

49. 689 N.E.2d 1265 (Ind. Ct. App. 1998).

50. *See* IND. CODE § 29-1-2-6 (1998). That section provides:

> Descendants of the intestate, begotten before his death but born thereafter, shall inherit as if they had been born in the lifetime of the intestate and had survived him. With this exception, the descent and distribution of the intestate estates shall be determined by the relationships existing at the time of the death of the intestate.

Id.

51. *See id.* § 31-14-7-1(1)(A) & (B).

52. *See id.* § 29-1-2-1(d)(1).

within five months of the decedent's death.[53] Additionally, he argued, the presumption that a child born during a marriage is the biological child of the father may be rebutted by direct, clear, and convincing evidence[54] and blood test results could provide the necessary evidence.[55]

The trial court ordered the blood tests, but the court of appeals, in an opinion construing probate and paternity law, reversed the trial court's judgment and vacated the order for paternity blood testing.[56] The court of appeals, while recognizing the uncle's standing as a potential heir[57] to petition the court to determine heirship,[58] nonetheless found that this did not automatically give the uncle standing to petition the court to order paternity blood testing.[59] Facts working against the uncle were that he was not claiming to be the putative father of the child and that he was attempting to disestablish paternity of a child born into an intact marriage.

The court rejected the uncle's use of Indiana Code section 29-1-2-7 as a

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53. *See Lamey*, 689 N.E.2d at 1270; *see also* IND. CODE § 29-1-2-7(b) (1998). That section provides:

> For the purpose of inheritance (on the paternal side) to, through, and from a child born out of wedlock, the child shall be treated as if the child's father were married to the child's mother at the time of the child's birth, if:
>
> (1) the paternity of the child has been established by law in a cause of action that is filed:
>
> (A) during the father's lifetime; or
>
> (B) within five (5) months after the father's death; or
>
> (2) the putative father marries the mother of the child and acknowledges the child to be his own.

Id.

54. *See Lamey*, 689 N.E.2d at 1268. In support of his argument, the uncle pointed to the holding in *K.S. v. R.S.*, 669 N.E.2d 399 (Ind. 1996), that a "child born to a married woman, but fathered by a man other than her husband, is a 'child born out of wedlock' for purposes of the [paternity] statute." *Id.* at 402 (permitting a third party's action to seek to establish his paternity in a child born of an intact marriage), *noted in* Paula J. Schaefer & Michael G. Ruppert, *Indiana Survey of Family Law in 1996*, 30 IND. L. REV. 1073, 1095 (1997).

55. *See* IND. CODE § 31-14-7-1(4) (1998).

56. *Lamey*, 689 N.E.2d at 1270. A concurring judge agreed with the majority that the trial court abused its discretion, but sought to limit the result to facts similar to this case. Precisely, a third party should not be allowed to challenge the paternity of a child born during an intact marriage where the decedent-father was conclusively bound to the establishment of paternity because he acknowledged paternity in a divorce decree dissolving the marriage. *See id.* (Kirsch, J., concurring in result). However, this judge was reluctant to conclude along with the majority that under no circumstances could the heirship of a child born during an intact marriage be challenged. *Id.*

57. *See* IND. CODE § 29-1-2-1(d)(3) (1998).

58. *See id.* § 29-1-6-6-(a). This section provides, in pertinent part: "At any time during the administration of a decedent's estate . . . any interested person may petition the court to determine the heirs of said decedent and their respective interests in the estate or any part thereof . . . ." *Id.*

59. *Lamey*, 689 N.E.2d at 1268.

vehicle for asserting his request, finding that the statute merely offered a limited opportunity to an illegitimate child or a putative father to establish paternity in a decedent, as opposed to third parties attempting to disestablish paternity following a presumptive father's death.[60] Moreover, the court found that the uncle, who was not claiming to be the child's biological father, had no standing under Indiana paternity law to establish or disestablish the child's paternity.[61] Specifically, the court refused to extend the recent Indiana Supreme Court holding in *K.S. v. R.S.*,[62] permitting a putative father's action to establish paternity in a child of a intact marriage, to a third party who is not claiming paternity but is trying to illegitimatize a child so that he may become eligible to inherit the father's estate.[63]

E. Claims Against the Estate

Two Indiana Court of Appeals decisions handed down during the survey period underscore the necessity that to perfect a tort claim against a deceased tortfeasor's estate, the complaint must be filed against the personal representative of the estate within the tort statute of limitations and, if the estate has not already been opened and/or a personal representative not yet appointed, the onus is on the tort claimant to accomplish this before the statute of limitations has run.[64]

In *Clark v. Estate of Slavens*,[65] the court upheld summary judgment in favor of the estate when a tort claimant failed to open an estate and seek appointment of a personal representative within the limitations period of the applicable tort statute.[66] The day before the expiration of the two-year statute of limitations, the

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60. *Id.* The court also noted that paternity had been established and conclusively bound the decedent and the former wife upon their divorce when they had agreed to the finding in the divorce decree that the child was born of the marriage. *Id.* at 1269.

61. *Id.* at 1268-70.

62. 669 N.E.2d 399 (Ind. 1996). *See also supra* note 54.

63. *Lamey*, 689 N.E.2d at 1270.

64. *See* Indiana Farmer's Mut. Ins. Co. v. Richie, 694 N.E.2d 1220 (Ind. Ct. App. 1998); Clark v. Estate of Slavens, 687 N.E.2d 246 (Ind. Ct. App. 1997).

65. 687 N.E.2d 246 (Ind. Ct. App. 1997).

66. Providing for the filing of claims against a decedent's estate, Indiana Code section 29-1-14-1 mandates, in pertinent part:

> (a) Except as provided in [Indiana Code section] 29-1-7-7, all claims against a decedent's estate, other than expenses of administration and claims of the United States, the state, or a subdivision of the state, whether due or to become due, absolute or contingent, liquidated or unliquidated, founded on contract or otherwise, shall be forever barred against the estate, the personal representative, the heirs, devisees, and legatees of the decedent, unless filed with the court in which such estate is being administered within:
>
> (1) Five (5) months after the date of the first published notice to creditors; or
>
> (2) Three (3) months after the court has revoked probate of a will, in

tort claimant filed a lawsuit against the estate of the decedent, simply named in the complaint as "Estate of Andrea E. Slavens,"[67] her brother, and her parents[68] for injuries sustained in an automobile accident caused by the driver of the defendants' vehicle. However, no estate existed at that time, and the estate could not be a party to the action without a personal representative.[69] Only after the expiration of the two-year statute of limitations did the tort claimant attempt to open an estate for the decedent, requesting that her attorney be appointed as the decedent's personal representative.[70] The court of appeals held that the tort claimant no longer had a viable claim against the decedent's estate[71] and was no

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> accordance with [Indiana Code section] 29-1-7-21, if the claimant was named as a beneficiary in that revoked will; whichever is later.
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> * * *
>
> (d) All claims barrable under subsection (a) shall be barred if not filed within one (1) year after the death of the decedent.
>
> * * *
>
> (f) Nothing in this section shall affect or prevent the enforcement of a claim for injury to person or damage to property arising out of negligence against the estate of a deceased tort feasor within the period of the statute of limitations provided for the tort action. A tort claim against the estate of the tort feasor may be opened or reopened and suit filed against the special representative of the estate within the period of the statute of limitations of the tort. Any recovery against the tort feasor's estate shall not affect any interest in the assets of the estate unless the suit was filed within the time allowed for filing claims against the estate. The rules of pleading and procedure in such cases shall be the same as apply in ordinary civil actions.

IND. CODE § 29-1-14-1 (1998). *See also* IND. CODE § 34-1-2-2(1) (1998) (defining statute of limitations for injuries to person, character, or personal property as two years).

67. *Clark*, 687 N.E.2d at 248.

68. *See id.* Unsure of who had been driving the defendants' car when the accident occurred, the tort claimant named the decedent and her brother, the occupants of the defendants' car, as defendants. The decedent's mother and father were also named as defendants because, pursuant to Indiana Code section 9-24-9-4(a) (1998), *see infra* note 75, the mother had agreed to be jointly and severally responsible for any liability the deceased might incur and the father had agreed to be jointly and severally responsible for any liability the brother might incur. *See Clark*, 687 N.E.2d at 248.

69. *See Clark*, 687 N.E.2d at 250 (citing 1 DEBRA A. FALENDER, HENRY'S INDIANA PROBATE LAW AND PRACTICE § 601 (8th ed. 1989)); *see also* Pasley v. American Underwriters, Inc., 433 N.E.2d 838 (Ind. Ct. App. 1982), *noted in* Debra A. Falender, *Trusts and Decedents' Estates*, 17 IND. L. REV. 387, 389-90 (1984); Carr v. Schneider's Estate, 51 N.E.2d 392 (Ind. App. 1943).

70. *See* Clark, 687 N.E.2d at 250. Indiana Code section 29-1-7-4 provides in pertinent part: "Any interested person . . . may petition the court having jurisdiction of the administration of the decedent's estate . . . [f]or the appointment of an administrator for the estate of any person dying intestate." IND. CODE § 29-1-7-4 (1998). *See also id.* § 29-1-1-3 (stating that "[i]nterested persons" include anyone "having a property right in or claim against the estate of a decedent being administered").

71. *Clark*, 687 N.E.2d at 250. The court quoted:

longer an "interested person" who had standing to open an estate.[72] Furthermore, because the tort claimant did not have standing to open an estate for the decedent, the estate could not be given legal recognition, and the tort claimant's attempt to substitute the "Estate's" personal representative for the party defendant "Estate of Andrea E. Slavens" in her complaint also had no effect.[73]

The tort claimant's failure to take timely action to open an estate and appoint a personal representative also caused the *Clark* court to affirm summary judgment in the mother's favor.[74] The mother had been named as a party in the tort claimant's complaint because she had agreed to be jointly and severally responsible for the liability of the decedent under Indiana Code section 9-24-9-4(a).[75] Inasmuch as the statute only provided for responsibility in the event that the minor decedent was liable in damages[76] and summary judgment had been granted in favor of the minor decedent's estate, the court found that the mother could not be held liable for the decedent's negligence.[77] Interestingly, the court stated in dicta that the tort claimant would also be barred from bringing an action against the mother based on grounds that she might be in possession of the

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> [Indiana Code 29-1-14-1(f)] allows a claimant to open the decedent tortfeasor's estate during the applicable tort statute of limitations. Therefore, as long as the estate of a decedent torfeasor is opened and a personal representative appointed within the statute of limitations, a tort action is not barred.

Id. (quoting Langston v. Estate of Cuppels, 471 N.E.2d 17, 20 (Ind. Ct. App. 1984)) (alteration in original).

72. *Id.*

73. *See id.* at 248-50. The amended complaint failed to relate back to the date of the filing of the original complaint under Indiana Rule of Trial Procedure 15(C). *See id.* at 250. *Compare id. with* Zambrana v. Anderson, 549 N.E.2d 1078 (Ind. Ct. App. 1990) (permitting the tort claimant to amend the complaint to name the estate as a party after the tort statute of limitations had run and the amendment related back to the filing of the original complaint because the requirements of Rule 15(C) had been satisfied when, prior to the expiration of the statute of limitations: 1) the estate had been opened; 2) the original complaint had been filed; 3) a special representative for purposes of proceeding with the tort action had been appointed and had received service of the summons and complaint for the tort; and 4) both the special representative and insurer for the decedent had timely notice of the action and knew that but for the mistake concerning the proper identity of the party the complaint would have been brought against the special representative).

74. *Clark*, 687 N.E.2d at 250-51. The *Clark* court also affirmed summary judgment in favor of the brother and father on other grounds. *See id.* at 251-56.

75. *See id.* at 250. Indiana Code section 9-24-9-4(a) provides:

> An individual who signs an application for a permit or license under this chapter agrees to be responsible jointly and severally with the minor applicant for any injury or damage that the minor applicant causes by reason of the operation of a motor vehicle if the minor applicant is liable in damages.

IND. CODE § 9-24-9-4(a) (1998).

76. *Clark*, 687 N.E.2d at 251 (citing Wenisch v. Hoffmeister, 342 N.E.2d 665, 667 (Ind. Ct. App. 1976)).

77. *Id.*

deceased's property. "'Only a duly authorized personal representative'" can recover the assets of an heir in possession and only such a representative can collect the assets in payment of any debts excepted under Indiana Code section 29-1-14-1(f).[78]

A later decision in the survey period, *Indiana Farmers Mutual Ins. Co. v. Richie*,[79] involved a situation similar to *Clark*. Immediately before the expiration of the statute of limitations, the tort claimant filed a complaint against "Leanne M. Smith, (deceased)," who had been involved in a automobile accident with the claimant that resulted in her death and injury to the claimant.[80] Three months later, the tort claimant petitioned for the appointment of a special administrator for the decedent's estate, and the estate was opened that day with an appointed administrator. In addition, the tort claimant moved to amend his complaint to change the named defendant to the special administrator for the deceased's estate. Tracking the same reasoning used by the *Clark* court, the *Richie* court reversed the trial court's judgment and granted summary distribution against the tort claimant.[81] A majority of the court held that the estate could not be given legal recognition and that the tort claimant's attempt to substitute the named defendant in an effort to "save" his claim was to no avail.[82] Relying on *Clark*, the court stated that, after the expiration of the statute of limitations, the tort claimant did not have standing to open an estate or petition for appointment of an administrator because he was no longer an "interested person."[83]

F. *Statutory Amendment*

Effective July 1, 1998, Indiana Code section 29-1-8-3, providing for the summary closing of a small estate, applies to a gross estate, which, less liens and encumbrances, does not exceed $25,000 plus administration costs and funeral expenses.[84] With this recent amendment, the general assembly continues what

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78. *Id.* (quoting 1 FALENDER, *supra* note 69, § 405).

79. 694 N.E.2d 1220 (Ind. Ct. App. 1998).

80. *See id.* at 1221.

81. *Id.* at 1223.

82. *Id.* The dissenting judge did not agree that Indiana Code section 29-1-14-1(f) barred the tort claimant's action to the extent he sought "to realize upon any casualty insurance proceeds available to indemnify against decedent's negligence, and does not seek to affect any interest in the assets of the estate." *Id.* (Bailey, J., dissenting).

83. *Id.* at 1223.

84. Act of March 11, 1998, Pub. L. No. 42-1998, § 2, 1998 Acts 1038 (codified as amended at IND. CODE § 29-1-8-3 (1998)). Indiana Code section 29-1-8-3 now provides, in pertinent part:

> (a) If it appears that the value of a decedent's gross probate estate, less liens and encumbrances, does not exceed the sum of:
>
> (1) twenty-five thousand dollars ($25,000);
>
> (2) the costs and expenses of administration; and
>
> (3) reasonable funeral expenses;
>
> the personal representative or a person acting on behalf of the distributees, without

now appears to be an ineffective attempt, beginning with a 1997 amendment, to relax the conditions under which summary distribution of an estate will be allowed.

Prior to the 1997 amendment, section 29-1-8-3 provided for summary distribution only when the gross probate estate, less liens and encumbrances, did not exceed the survivor's allowance, if any was payable, plus administration costs and funeral expenses. This meant that summary distribution of an estate was limited to situations where distribution would be made to a surviving spouse or dependent children claiming the survivor's allowance, cost claimants, and/or funeral claimants. The 1997 legislature amended section 29-1-8-3 by substituting the amount of $15,000 for the survivor's allowance in the equation.[85] However, the survivor's allowance, although no longer specifically referenced in the amendment, still could have been construed as representing the figure of $15,000 because the 1997 legislature also the amended the amount of the survivor's allowance provided under section 29-1-4-1 to $15,000.[86] In addition, section 29-

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> giving notice to creditors, may immediately disburse and distribute the estate to the persons entitled to it and file a closing statement as provided in section 4 of this chapter.
>
> (b) If an estate described in subsection (a) includes real property, an affidavit may be recorded in the office of the recorder in the county in which the real property is located. The affidavit must contain the following:
>
> * * *
>
>> (2) The following statement: "It appears that the decedent's gross estate, less lien and encumbrances, does not exceed the sum of the following: twenty-five thousand dollars ($25,000), the costs and expenses of administration, and reasonable funeral expenses."
>
> * * *

IND. CODE § 29-1-8-3.

85. Act of May 13, 1997, Pub. L. No. 118-1997, § 17, 1997 Acts 1284 (codified as amended at IND. CODE § 29-1-4-1 (1998)).

86. Act of May 13, 1997, Pub. L. No. 118-1997, § 11, 1997 Acts 1284 (codified as amended at IND. CODE § 29-1-4-1 (1998)). Indiana Code section 29-1-4-1, as amended to clarify wording, provides:

> The surviving spouse of a decedent who was domiciled in Indiana at his death is entitled from the estate to an allowance of fifteen thousand dollars ($15,000). The allowance may be claimed against the personal property of the estate or a residence of the surviving spouse, or a combination of both. If there is no surviving spouse, the decedent's children who are under eighteen (18) years of age at the time of the decedent's death are entitled to the same allowance to be divided equally among them. If there is less than fifteen thousand dollars ($15,000) in personal property in the estate and residence of the surviving spouse, the spouse or decedent's children who are under eighteen (18) years of age at the time of the decedent's death, as the case may be, are entitled to any real estate of the estate to the extent necessary to make up the difference between the value of the personal property plus the residence of the surviving spouse and fifteen thousand dollars ($15,000). The amount of that difference is a lien on the

1-8-4(a), which remained unamended, mandates that, in order to close the estate, the personal representative must file an affidavit with the court stating, among other items, that the gross probate estate, less liens and encumbrances, does not exceed *the allowance provided under section 29-1-4-1*, administration costs, and funeral expenses.[87]

During the current survey period, the legislature once again amended section 29-1-8-3, this time to permit summary distribution if the gross probate estate, less liens and encumbrances, does not exceed $25,000, an amount now exceeding the survivor's allowance, administration costs, and funeral expenses.[88] Thus, section 29-1-8-3 now provides that a summary distribution of an estate could be made even in situations where heirs of a decedent's estate might receive assets beyond the survivor's allowance. Nevertheless, section 29-1-8-3, as newly amended, now conflicts with section 29-1-8-4, which remains unamended. Therefore, despite the apparent attempt by the legislature to ease the restrictions for the summary distribution and closing of a small estate, it appears that for now such procedures are still limited to those estates that, less liens and encumbrances, are not in excess of the survivor's allowance, administration costs, and funeral expenses.

II. INHERITANCE TAX

In order to make a valid qualified terminable interest property ("QTIP") election for Indiana inheritance tax purposes,[89] a QTIP election form, as

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> remaining real estate. An allowance under this section is not chargeable against the distributive shares of either the surviving spouse or the children.

IND. CODE § 29-1-4-1.

87. Indiana Code section 29-1-8-4(a) provides, in pertinent part:

> Unless prohibited by order of the court and except for estates being administered by supervised personal representatives, a personal representative or a person acting on behalf of the distributees may close an estate administered under the summary procedures of section 3 [Indiana Code section 29-1-8-3] of this chapter by filing with the court, at any time after disbursement and distribution of the estate, a verified statement stating that:
>
> (1) to the best knowledge of the personal representative, or person acting on behalf of the distributees the value of the gross probate estate, less liens and encumbrances, did not exceed the sum of:
>
> (A) the allowance, if any provided by [Indiana Code section] 29-1-4-1;
>
> (B) the costs and expenses of administration; and
>
> (C) reasonable funeral expenses[.]
>
> * * *

IND. CODE § 29-1-8-4(a) (1998).

88. Act of March 11, 1998, Pub. L. No. 42-1998, § 2, 1998 Acts 1038 (codified as amended at IND. CODE § 29-1-8-3 (1998)). *See supra* note 84.

89. *See* IND. CODE § 6-4.1-3-7(a) (1998). This section provides that a decedent's property interests passing to the surviving spouse are exempt from Indiana inheritance tax. This includes

prescribed by Indiana Department of State Revenue ("IDSR") regulations, must be attached to the inheritance tax return.[90] However, the estate in *Department of State Revenue v. Estate of Phelps*[91] initially attempted to make a QTIP election by attaching the decedent's will and revocable trust agreement to the return. In the 1994 decision of *Estate of Hibbs v. Indiana Department of State Revenue*,[92] the tax court found the attachment to the return of a decedent's will and trust, which contained directives unequivocally commanding the personal representative to make the QTIP election, satisfied the statutory requirements of a writing for purposes of making the election.[93] Unfortunately, after the decision in *Hibbs* but before the decedent's death in *Phelps*, the IDSR regulation prescribing the form and content of a QTIP election came into effect.[94] Thus, the attachment of the will and trust to the inheritance tax return in *Phelps* was an ineffective election.[95]

The estate attempted to rectify its mistake and salvage the election by filing a second inheritance tax return, with the appropriate QTIP election form attached, prior to the due date of the return. In an attempt to circumvent the requirement that the QTIP election be "attached to the *original* Indiana inheritance tax return,"[96] the estate argued this language should be interpreted to

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the transfer of a life estate to the surviving spouse. *Id.* § 6-4.1-3-7(b). But the transfer of the remainder interest is usually subject to inheritance tax, which can be postponed or avoided by making a QTIP election pursuant to Indiana Code section 6-4.1-3-7(c) (1998). Indiana Code section 6-4.1-3-7(d) mandates, in part, that the election must be in writing and attached to the inheritance tax return, if one is required to be filed. IND. CODE § 6-4.1-3-7(d) (1998).

90. *See* IND. ADMIN. CODE tit. 45, r. 4.1-3-5(b)(4) (1996). That section provides:

The election must be in form and content substantially as follows:

> Pursuant to [Indiana Code section] 6-4.1-3-7, an election is hereby made to treat the following property passing from the decedent in which the surviving spouse has a qualifying income interest for life as a property interest which a decedent transfers to the decedent's surviving spouse:
>
> | Qualified Property | Percentage |
> |---|---|
> | __________________ | ____________ |
> | __________________ | ____________ |
>
> It is understood that this QTIP election is irrevocable and cannot be reversed.
>
> Signature ____________________________
>
> Title _______________________________

Id.

91. 697 N.E.2d 506 (Ind. Tax Ct. 1998).

92. 636 N.E.2d 204 (Ind. Tax Ct. 1994).

93. *Id.* at 210.

94. *See Phelps*, 697 N.E.2d at 510 n.4. Title 45, rule 4.1-3-5 of the Indiana Administrative Code became effective on July 1, 1994. IND. ADMIN. CODE tit. 45, r. 4.1-3-5 (1996).

95. *See Phelps*, 697 N.E.2d at 510.

96. IND. ADMIN. CODE tit. 45, r. 4.1-3-5(b)(3) (emphasis added). That rule prescribes: "The

include supplemental inheritance tax returns, that is, a second return filed before the due date of the return.[97] The court, admitting that it was not without sympathy for the estate's position, acknowledged the IDSR regulations were "unnecessarily inconsistent with federal regulations governing federal estate tax returns" and that it could see no harm in allowing the filing of amended returns adding the QTIP election before the due date.[98] Also, the court pointed out an inconsistency between Indiana Code section 6-4.1-3-7(d), which reflects the possibility of a valid QTIP election in some instances without the filing of a inheritance tax return,[99] and the IDSR regulation, which requires the filing of an inheritance tax return for a QTIP election.[100] Further, the court noted that the IDSR regulation does not prohibit a QTIP election in a late filed initial return, which gives the effect of treating late filed initial returns more favorably than timely filed amended returns.[101] Yet, despite parading these inconsistencies and inequities, the court in the end declined to do anything except to enforce the will of the IDSR as expressed in its regulation.[102] Therefore, when the inheritance return initially filed does not contain the necessary QTIP election form, an estate cannot salvage the QTIP election by filing a subsequent inheritance tax return containing the proper election form.[103]

III. TRUSTS

The court of appeals in *Regan v. Uebelhor*,[104] addressed the issue of whether a contingent remainderman of a testamentary trust was an interested party bound by a decree of final settlement in the decedent's estate with regard to the sale of an estate asset made during the administration of the estate. In addition, the court addressed whether the contingent remainderman had standing to sue the trustee regarding income earned from trust assets.

The contingent remainderman's grandfather died in 1977, leaving a will that named her uncle as executor of the estate and trustee of the trust created under

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election must be in writing, signed by a person authorized to make the election, and attached to the original Indiana inheritance tax return at the time it is filed." *Id.* Further, title 45, rule 4.1-3-5(e) of the Administrative Code prescribes: "The failure to comply with subsection (b) as to any property that would qualify under Section 2056(b)(7) of the Internal Revenue Code means that an irrevocable election has been made not to treat the transfer as a QTIP transfer." IND. ADMIN. CODE tit. 45, r. 4.1-3-5(e) (1996).

97. *See Phelps*, 697 N.E.2d at 510.

98. *Id.* at 511.

99. Indiana Code section 6-4.1-3-7(d) mandates: "The election referred to in subsection (c) shall be made in writing and shall be attached to the inheritance tax return, *if one is required to be filed.* The election, once made, is irrevocable." IND. CODE § 6-4.1-3-7(d) (1998) (emphasis added).

100. *Phelps*, 697 N.E.2d at 511 (referring to IND. ADMIN. CODE tit. 45, r. 4.1-3-5(d) (1996)).

101. *Id.*

102. *Id.* (referring to IND. ADMIN. CODE tit. 45, r. 4.1-3-5(e) (1996)).

103. *See id.*

104. 690 N.E.2d 1222 (Ind. Ct. App. 1998).

the will.[105] The will also gave the uncle the exclusive right to purchase the grandfather's interest in an automobile dealership from the estate. Later in 1977, the uncle, acting in his capacity as executor of the estate, petitioned the probate court for authority to sell the grandfather's share of the dealership to himself. He also filed the necessary consents to the transaction, signed by the grandfather's widow (grandmother to the contingent remainderman) and the grandfather's daughter (mother to the contingent remainderman).[106] That same year the probate court approved the sale, and the uncle purchased the grandfather's interest in the dealership from the estate. The grandfather's estate was not closed until 1986. In 1987, the probate court entered an order approving the final distribution of the grandfather's estate and discharging the uncle as executor.[107]

The testamentary trust established under the grandfather's will was not funded until the closing of the estate. Under the provisions of the testamentary trust, all income was to be paid to the contingent remainderman's grandmother for life and the trustee was given the power to invade the principal, if necessary, for the benefit of the grandmother.[108] Upon the grandmother's death, the assets remaining after a lump sum payment to another named remainder beneficiary were to be distributed in equal shares, one-half to the uncle and one-half to the uncle, as trustee, for the benefit of the contingent remainderman's mother. After the mother's death, any remaining trust property held for her benefit was to be distributed to her children, which turned out to be the contingent remainderman involved in this lawsuit. The mother predeceased the grandmother, who, in turn, died in 1993.[109]

In 1995, the contingent remainderman filed a complaint against her uncle, alleging he breached his fiduciary duty when he purchased her grandfather's one-half interest in an automobile dealership from the estate below the market price and when he borrowed money from the estate and trust below the market interest rate.[110] Despite receiving two checks from the trust in 1993, the contingent remainderman claimed that she was not aware of the trust or her interest therein until March 1994. The trial court dismissed her complaint, and the court of appeals affirmed the dismissal.[111]

The court of appeals first addressed the claim relating to the uncle's purchase of the grandfather's one-half interest in the automobile dealership. The court

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105. *See id.* at 1223.

106. *See id.*

107. *See id.* at 1224.

108. *See id.* The relevant trust provision stated:

> The trustee shall distribute to or on behalf of my wife during her lifetime all income and so much of the principal of the Trust as shall be necessary to provide my said wife with expenses of health, education, support or mode of living enjoyed by our family at the time of my death.

Id. at 1223.

109. *See id.* at 1224.

110. *See id.*

111. *Id.* at 1225-26.

rejected the contingent remainderman's argument that her cause of action against the uncle for breach of his fiduciary duty did not accrue until she first learned of the trust.[112] Under Indiana law a decree in final settlement of a decedent's estate is a final judgment that binds all interested parties and cannot be collaterally attacked more than one year after the judgment is rendered.[113] The court held that the contingent remainderman was an interested party bound by the final settlement of the grandfather's estate.[114]

In making its determination, the court relied primarily on Indiana Code section 30-4-6-10, which provides that an adjudication of a person's interest represented by a personal representative is binding on "'all interested persons, whether born or unborn, whether notified or not notified and whether represented or not'" when those persons "'have interests similar to the predominant interests of any person so notified or represented.'"[115] When the uncle petitioned the court for authority to sell the dealership, he was acting as the executor of the estate, not the trustee of the testamentary trust, and thus represented the grandmother and mother, who had the predominant interests.[116] Because the remainderman's interest derived from the grandmother's and mother's interests, the court held that her interest was similar to theirs.[117] Thus, she was bound to the probate adjudications approving the sale of the automobile dealership in 1977 and approving the distribution and closing of the estate in 1987.[118] Her complaint represented a collateral attack on these adjudications, and because she did not bring her claim within the one-year statute of limitations, the trial court properly dismissed this portion of her complaint.[119]

The court of appeals also affirmed dismissal of the remaining portion of the complaint because the contingent beneficiary lacked standing to sue the uncle for allegedly breaching his fiduciary duty when he borrowed money from the estate

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112. *Id.* at 1225. The contingent remainderman argued that her action was subject to a two-year statute of limitations as set forth in *Malachowski v. Bank One, Indianapolis*, 590 N.E.2d 559, 563 (Ind. 1992) (holding that the limitations period begins to run "when the plaintiff knew, or in the exercise of ordinary diligence could have discovered, that an injury had been sustained as a result of the tortious act of another").

113. *See id.* at 1224 (citing Apple v. Kile, 457 N.E.2d 254, 258 (Ind. Ct. App. 1983)).

114. *Id.* at 1225-26 (construing IND. CODE §§ 29-1-1-21, -17-13, -17-2(d), 30-4-6-10 (1998)).

115. *Regan*, 690 N.E.2d at 1225 (quoting IND. CODE § 30-4-6-10 (1998)).

116. *See id.*

117. *Id.*

118. *See id.* Indiana Code section 29-1-17-2(d) provides, in pertinent part:

> The decree of final distribution shall be a conclusive determination of the persons who are the successors in interest to the estate of the decedent and of the extent and character of their interest therein, subject only to the right of appeal the right to reopen the degree. It shall operate as the final adjudication of the transfer of the right, title and interest of the decedent to the distributees therein designated.

IND. CODE § 29-1-17-2(d) (1998).

119. *See Regan*, 690 N.E.2d at 1225.

and trust at an interest rate far below the market rate.[120] Because the terms of the trust required the uncle to distribute all the trust income to the grandmother, any increased amount of interest income generated from the trust property would have been distributed to the grandmother.[121] As a result, the grandmother would have been the only person who could have been injured by the uncle's loans at a below-market interest rate.[122] Additionally, the trust principal would not have significantly changed over the years unless the uncle, exercising his discretion as trustee, would have distributed all, or a portion, of the principal to satisfy the grandmother's needs.[123] Therefore, the contingent remainderman was unable to show the requisite direct injury to her interest resulting from the uncle's conduct.[124]

IV. Powers of Appointment

The legislature amended Indiana Code section 30-5-6-4(b), adding the heir or legatee of the principal to the list of those who can request an accounting from an attorney-in-fact and providing that a requested accounting must be submitted in writing.[125] Subsections (c), (d), and (e) were added to section 30-5-6-4.[126]

Subsection (c) mandates that the attorney-in-fact must deliver the accounting to the person making the request within sixty days after receipt of the written request.[127] Subsection (d) provides that, unless the court orders additional accountings, the attorney-in-fact is not required to render more than one requested accounting under section 30-5-6-4 during a twelve-month period.[128] Finally, subsection (e) provides that the person requesting the accounting may bring an action in mandamus to compel the attorney-in-fact to render an accounting in the event the attorney-in-fact fails to deliver the requested accounting within the sixty-day period.[129] Furthermore, the person requesting the accounting may be awarded attorney's fees and court costs incurred in connection with bringing such an action, if the court finds that the attorney-in-

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120. *Id.* at 1226.

121. *See id.*

122. *See id.*

123. *See id.*

124. *See id.* at 1225-26 (citing Schloss v. City of Indianapolis, 553 N.E.2d 1204, 1206 (Ind. 1990) (holding that the judiciary can only resolve disputes in which the complainant has sustained, or is "in immediate danger of sustaining," a direct injury resulting from the conduct at issue); Higgins v. Hale, 476 N.E.2d 95, 101 (Ind. 1985)).

125. Act of March 12, 1998, Pub. L. No. 77-1998, § 1, 1998 Acts 1165 (codified as amended at Ind. Code § 30-5-6-4(a) (1998)).

126. Act of March 12, 1998, Pub. L. No. 77-1998, §1, 1998 Acts 1165 (codified as amended at Ind. Code §§ 30-5-6-4(c) to (e) (1998)).

127. Ind. Code § 30-5-6-4(c).

128. *Id.* § 30-5-6-4(d).

129. *Id.* § 30-5-6-4(e).

fact failed to render the account without just cause.[130]

V. GUARDIANSHIPS

A. Disposition of Assets

In *In re Guardianship of Hall*,[131] the majority of the court held that distribution of a portion of the guardianship estate to the incapacitated husband's financially dependent wife was not an abuse of discretion pursuant to the doctrine of necessaries.[132] Shortly after their marriage but prior to the husband's incapacitation, the husband had insisted that his wife discontinue her employment, that he move into her home, and that he financially support her. Although the elderly husband, eighty-one years old at the time of the dispute, had only been married to the petitioning spouse for three years, the court found

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130. *See id.*

131. 694 N.E.2d 1168 (Ind. Ct. App. 1998).

132. *Id.* at 1170. While concurring that the trial court did not abuse its discretion in awarding the spouse monthly income from the ward's property, the dissenting judge did not agree with the majority's upholding of an additional $10,000 distribution because, unlike the monthly income award, there was no evidence establishing the spouse's need for the additional $10,000. *Id.* at 1171 (Hoffman, J., concurring in part and dissenting in part). Reasoning that the doctrine of necessaries permits an award to cover only those needs which the debtor spouse is unable to personally satisfy, the dissenting judge would have remanded for a statement justifying the spouse's need for the $10,000 or a vacation of the award. *Id.*

As a procedural note, the guardians argued on appeal that the trial court erred in granting the spouse's petition for a distribution of the assets based on the provisions of the Spousal Impoverishment Amendments of the Medicare Catastrophic Coverage Act (the "Act"), 42 U.S.C. § 1396 (1994 & Supp. II 1996). The *Hall* court noted that the petitioning spouse apparently conceded that the Act did not provide for a spouse's private right of action against the other spouse inasmuch as on appeal she did not claim that § 1396 gave her a private cause of action against the incapacitated spouse. *Hall*, 694 N.E.2d at 1169. Nevertheless, because neither party requested specific findings and conclusions and the trial court did not enter such findings and conclusions sua sponte, the *Hall* court concluded that "the trial court's judgment [was] a general one which [the court would] affirm on any theory supported by the evidence adduced at trial." *Id.* (citing DeKalb Chiropractic Ctr., Inc. v. Bio-Testing Innovation, Inc., 678 N.E.2d 412, 414 (Ind. Ct. App. 1997)). The *Hall* court affirmed the trial court's judgment based on the "doctrine of necessaries," which was supported by the evidence presented at trial. *Id.* at 1170.

Further, the *Hall* court noted that the petitioning spouse sought a distribution of the "marital" assets, and, if such were indeed the case, the court had no authority to distribute the marital assets in a guardianship proceeding. *Id.* Except in the case of a marital dissolution or in a more limited sense in a legal separation, no court action is required for either spouse to dispose of marital assets. *See id.* at 1169-70 (citing IND. CODE §§ 31-15-7-4, -4-8 (1998)). Regardless, the court established that the assets involved in this dispute belonged solely to the incapacitated spouse and were guardianship assets. *Id.* at 1170.

Indiana's doctrine of necessaries[133] applicable because the petitioning spouse was unable to meet her expenses with her own funds and was "dependent upon her financially superior spouse."[134]

B. Statutory Amendment

One statutory amendment enacted during the survey period is of interest in guardianships. Indiana Code section 29-3-3-1(a), providing for payment of a debt to a minor or delivery of a minor's property to any person having care or custody of the minor[135] without the appointment of a guardian, giving of bond or other court order, was amended to apply to debt or property not exceeding $5000 in value.[136]

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133. *Id.* (citing Bartrom v. Adjustment Bureau, Inc., 618 N.E.2d 1 (Ind. 1993), *noted in* Andrew Z. Soshnick, *Indiana Family Law 1993: Much Ado About Some Things, 1993 Survey of Recent Developments in Indiana Law*, 27 IND. L. REV. 1093, 1116-17 (1994); Sally A. Sager, *Family Law Case Update*, 37 RES GESTAE 280, 283 (Dec. 1993)). The court in *Bartrom* gave an exhaustive history of the doctrine of necessaries in Indiana and, synthesizing the law, held that the Indiana doctrine operated as follows:

> Each spouse is primarily liable for his or her independent debts. . . . When, however, there is a shortfall between a dependent spouse's necessary expenses and separate funds, the law will impose limited secondary liability upon the financially superior spouse by means of the doctrine of necessaries. We characterize the liability as "limited" because its outer boundaries are marked by the financially superior spouse's ability to pay at the time the debt was incurred. It is "secondary" in the sense that it exists only to the extent that the debtor spouse is unable to satisfy his or her own personal needs or obligations.

Bartrom, 618 N.E.2d at 8.

134. *Hall*, 694 N.E.2d at 1170.

135. In the guardianship code, a minor is a person less than eighteen years of age who is not emancipated. IND. CODE § 29-3-1-10 (1998).

136. Act of March 11, 1998, Pub. L. No. 42-1998, § 3, 1998 Acts 1038 (codified as amended at IND. CODE § 29-3-3-1(a) (1998)). The former statute only applied to debt or property not exceeding $3500 in value.

1998 SURVEY OF THE UNIFORM COMMERCIAL CODE IN INDIANA

HAROLD GREENBERG*

INTRODUCTION

This Article summarizes and comments upon recent developments of particular interest that affect the Uniform Commercial Code ("UCC") in Indiana.[1] In addition to Indiana state and federal cases, the discussion includes cases that the United States Court of Appeals for the Seventh Circuit has decided that originated in federal district courts in other states within the circuit. Although the latter cases will involve those states' application of the UCC, the decisions will control the federal district courts in Indiana on UCC issues that Indiana courts have not yet addressed.

I. ARTICLE 2—SALES

A. Seller's Remedy of Specific Performance; Insecurity, Assurances of Performance, and Anticipatory Repudiation (Sections 2-609; 2-610)

In *Jay County Rural Electric Membership Corp. v. Wabash Valley Power Ass'n*,[2] which is likely to be a leading case, the Indiana Court of Appeals stated that specific performance may be available to a seller as a remedy for a buyer's breach, notwithstanding that the UCC is silent on the matter.[3] In 1977, the rural electric company became a member of the power association cooperative and agreed to purchase from the cooperative all the electricity the electric company would require for a term ultimately extended through 2028. The federal predecessor to the Rural Utilities Service ("RUS") developed this type of "all-requirements" as the principal collateral for billions of dollars in loans to electrical cooperatives nationwide. As the court described: "The all-requirements contract between [the cooperative] and each of its members allows the members to develop, purchase, and secure generation and transmission resources without having to provide individual guarantees for the financing extended [by RUS] to [the cooperative]."[4] The rates the cooperative charged to

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* Professor of Law, Indiana University School of Law—Indianapolis. A.B., Temple University; J.D., University of Pennsylvania.

1. IND. CODE §§ 26-1-1 to -10 (1998). Unless the Indiana version of the UCC differs from the Official Draft of the UCC, the citation form used will be the generic form from the Official Draft rather than the full Indiana citation form, e.g., section 2-201 rather than section 26-1-2-201. The UCC, as enacted in other states, will also be cited in this generic form.

2. 692 N.E.2d 905 (Ind. Ct. App. 1998).

3. *Id.* at 913.

4. *Id.* at 908. This historical background of these all-requirements contracts is more fully described in *Tri-State Generation & Transmission Ass'n v. Shoshone River Power, Inc.*, 805 F.2d 351 (10th Cir. 1986). On appeal after remand, the court ruled that the sale of all of the assets of a member power company to a non-member would result in a change of the member's requirements

its members are set by a board consisting of one representative from each of the members.

In late 1996 and early 1997, the electric company sent notices to the cooperative that it would not nominate a representative to the board, was withdrawing from membership, and was terminating its all-requirements contract. The electric company then filed an action for declaratory judgment that its withdrawal and termination were valid and also signed a contract with another wholesale supplier for its requirements of electricity at lower prices than those set by the cooperative.[5] The cooperative responded with a motion for preliminary injunction that would require the electric company to continue purchasing its requirements of electricity from the cooperative at least until final judgment, in effect, granting specific performance temporarily. The trial court granted the preliminary injunction and granted the electric company leave to take an interlocutory appeal.[6]

1. The Availability of Specific Performance.—The issue of whether specific performance is available to a seller as a remedy for the buyer's breach is directly intertwined with two of the four requirements for obtaining a preliminary injunction: inadequate remedy at law and reasonable likelihood of success on the merits, the other two being balance of harm and the public interest.[7] Specific performance is traditionally an extraordinary remedy, and equitable in nature.[8] If money damages can suffice, neither an injunction nor specific performance is appropriate.[9] With respect to the likelihood of success on the merits, if the court were to conclude that specific performance is not available to a seller of goods, the request for preliminary injunction would fail.

The UCC expressly mentions the remedy of specific performance in only two instances and then only in the context of a buyer's remedies: first, in section 2-711, the index of the buyer's remedies, which lists specific performance as available "in a proper case,"[10] and, second, in section 2-716, which is captioned, "Buyer's Right to Specific Performance or Replevin," and states simply: "(1) Specific performance may be decreed where the goods are unique or in other

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of power under the all-requirements contract and constitute a violation of the contract. *Tri-State Generation & Transmission Ass'n v. Shoshone River Power, Inc.*, 874 F.2d 1349, 1360 (10th Cir. 1989). The court of appeals vacated the district court's denial of a permanent injunction against the sale and remanded for a new trial to determine if money damages would be adequate. *Id.* at 1364. If money damages were not calculable, the court stated that the injunction against the sale should be made permanent. *Id.* The issue of specific performance under UCC section 2-716 was not discussed.

5. *See Jay County Rural Elec. Membership*, 692 N.E.2d at 908.

6. *See id.*

7. *See id.* at 909.

8. *See generally* Harold Greenberg, *Specific Performance Under Section 2-716 of the Uniform Commercial Code: "A More Liberal Attitude" in the "Grand Style"*, 17 NEW ENG. L. REV. 321 (1981-1982).

9. *See id.*

10. U.C.C. § 2-711(2)(b).

proper circumstances."[11] The only remedy expressly available to a seller that approaches specific performance is the seller's right to recover the price of the goods, section 2-709. This remedy has sometimes been called "a specific performance remedy," apparently because, in most cases, the seller's only interest is in compelling the buyer to perform by paying for the goods.[12] As White and Summers state: "The action for the price is, of course, the analogue to the buyer's action for specific performance."[13]

In *Jay County*, the court of appeals agreed with the trial court that in an appropriate case, a seller may be entitled to specific performance.[14] In reaching its decision, the court relied on the reasoning of *Central Illinois Public Service Co. v. Consolidated Coal Co.*,[15] which was quite similar in its facts. In *Consolidated Coal*, the electric company had agreed in 1962 to buy from the coal company all of its requirements of fuel for one of its generating stations; the contract was ultimately extended through 1995. One aspect of the complex litigation between the parties was the coal company seller's request for an order of specific performance against the electric company buyer. In reaching its decision in favor of the seller, the court referred to several pre-UCC cases in which the facts supported a decree of specific performance in favor of a seller.[16] The court noted that section 2-703 is not an exclusive list of seller's remedies,[17] and that, although the seller's action for the price pursuant to section 2-709 may equate an action for specific performance, a court may award an order of specific performance to a seller in unusual circumstances.[18] The circumstances in *Consolidated Coal* consisted of the contract between the parties, which contained many features of a joint venture, particularly because the power company station was located at the mouth of the mine, and the closure of the mine as a consequence of the contract termination would put hundreds of workers out of work.[19]

The Indiana Court of Appeals agreed with the *Consolidated Coal* court that while specific performance is not enumerated in the index of a seller's remedies in section 2-703, neither is it prohibited as a remedy.[20] Further, the court noted

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11. *Id.* § 2-716(1).

12. *See* Central Ill. Pub. Serv. Co. v. Consolidated Coal Co., 527 F. Supp. 58, 64-65 (C.D. Ill. 1981), *aff'd & remanded*, 673 F.2d 1333 (7th Cir. 1981); John E. Murray, Jr., *The Emerging Article 2: The Latest Iteration*, 35 DUQ. L. REV. 533, 611 (1997).

13. 1 JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 7-2 n.2 (4th ed. 1995).

14. *Jay County Rural Elec. Membership*, 692 N.E.2d at 913.

15. 527 F. Supp. 58 (C.D. Ill. 1981), *aff'd & remanded*, 673 F.2d 1333 (7th Cir. 1981).

16. *Id.* at 65 (citing United Fuel Gas Co. v. Columbian Fuel Corp., 165 F.2d 746 (4th Cir. 1948); Allen W. Hinkel Dry Goods Co. v. Wichison Indus. Gas Co., 64 F.2d 881 (10th Cir. 1933); Oklahoma Natural Gas Corp. v. Municipal Gas Co., 38 F.2d 444 (10th Cir. 1930)).

17. *Id.* at 64-65.

18. *Id.* at 65.

19. *Id.* at 64.

20. *Jay County Rural Elec. Membership*, 692 N.E.2d at 913.

that section 1-103 preserves principles of law and equity as supplemental to the UCC in the absence of a contrary provision.[21] In proper circumstances, where an award of money damages would not sufficiently protect the aggrieved seller, a decree of specific performance is appropriate.[22]

The *Jay County* court continued that the uniqueness of the interrelationship of the power association cooperative with its members, the relation of the cooperative with RUS, the length of the contract, as well as the probable inability of the electric company to pay huge but presently unquantifiable damages, justified the grant of the preliminary injunction (and might support a final judgment granting specific performance).[23]

The court's position is sound. Section 1-102 states that the UCC "shall be liberally construed and applied to promote its underlying purposes and policies," two of which are "to simplify, clarify and modernize the law governing commercial transactions; [and] to permit the continued expansion of commercial practices through custom, usage and agreement of the parties."[24] Further, the UCC's remedies "shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed . . . ."[25] Taking these provisions together with section 1-103, and considering the preliminary findings of the insufficiency of money damages coupled with the irreparable harm to the cooperative, specific performance appears to be the only remedy that would achieve the goals that underlie the UCC.

The drafters of the revised Article 2 appear to agree. In the December 1993 draft, specific performance remained a buyer's remedy. In commenting on the draft's section 2-709, "Action for the Price," the reporter stated: "The current version of Article 2 says nothing about a seller's right to specific performance. This remedy is not displaced by Section 2-709 and, presumably, is still available under Section 1-103."[26] In the note to section 2-716, "Buyer's Right to Specific Performance or Replevin," the reporter stated:

> The Drafting Committee agreed with the Study Group that specific performance should be available to the buyer if the parties have expressly agreed. . . . The Drafting Committee, however, rejected a proposal that similar language should be included for the seller. As it now stands, a seller's right to specific performance depends upon

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21. *Id.* UCC section 1-103 states: "Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions." U.C.C. § 1-103.

22. *Jay County Rural Elec. Membership*, 692 N.E.2d at 913.

23. *Id.*

24. U.C.C. §§ 1-102(1), (2).

25. *Id.* § 1-106(1).

26. *Id.* § 2-709, Reporter's Notes, Note 3 (Dec. 21, 1993 Draft) (copy on file with the *Indiana Law Review*).

equitable principles not displaced by Article 2. See Section 1-103.[27]

The drafters have since changed their position. At least since 1996, the revised versions of Article 2 under consideration have authorized an award of specific performance to either the buyer or the seller.[28] By using the phrase "the agreed performance of the party in breach[,]"[29] new section 2-807 "recognizes that performance other than the goods may be unique."[30] As the drafters observed in 1996: "A seller may obtain specific performance of the buyer's agreement to accept and to pay for the goods in appropriate cases. This simply affirms what some courts have always done, especially in long term supply contracts."[31] As one scholar states: "There are a number of cases, dating from almost a century ago to the present, in which a long-term supply contract has been specifically enforced because determination of damages was deemed too speculative."[32]

Thus, it appears that, at least preliminarily, the order that the electric company continue to take its requirements from the cooperative is in accord with the philosophy underlying the UCC and the thinking of the experts involved in its revision. The cooperative still has the burden of proving that its remedy at law for money damages is inadequate, but that is a matter for the trial on the merits. If the cooperative can prove that this is one of the unusual cases in which money damages will not be an adequate remedy for the buyer's breach, no good reason exists for the denial of the specific performance remedy.

2. *Insecurity, Assurances, and Anticipatory Repudiation.*—Another argument the electric company made in *Jay County* was that the power cooperative had repudiated the contract when the latter announced its desire to merge with another cooperative.[33] Although both cooperatives had adopted resolutions supporting the merger, at the time the electric company filed its

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27. *Id.* § 2-716, Reporter's Notes (Dec. 21, 1993 Draft) (copy on file with the *Indiana Law Review*).

28. *See id.* §§ 2-807 (May 1, 1998 Draft), 2-707 (Mar. 1, 1996 Draft), and the respective notes to each. *Id.* §§ 2-807 (May 1, 1998 Draft), 2-707 (Mar. 1, 1996 Draft), *available in* National Conference of Commissioners on Uniform State Laws, *Drafts of Uniform & Model Acts* (visited Mar. 25, 1998) <http://www.law.upenn.edu/bll/ulc/ulc.htm> [hereinafter *Draft Acts*]. The more recent of these sections states, in part:

> A court may enter a decree for specific performance if the parties have expressly agreed to that remedy of the goods or the agreed performance of the party in breach of contract are unique or in other proper circumstances. Even if the parties expressly agree to specific performance, a court shall not enter a decree for specific performance where the breaching party's sole remaining contractual obligation is the payment of money.

Id. § 2-807(a) (May 1, 1998 Draft), *available in Draft Acts*, *supra*.

29. *Id.* § 2-807 (May 1, 1998 Draft), *available in Draft Acts*, *supra* note 28.

30. *Id.* § 2-807, Note 1 (May 1, 1998 Draft), *available in Draft Acts*, *supra* note 28.

31. *Id.* § 2-707, Note 1 (Mar. 1, 1996 Draft), *available in Draft Acts*, *supra* note 28.

32. Gregory M. Travalio, *Measuring Seller's Damages for Breach of Long-Term Gas Purchase Contracts*, 14 E. MIN. L. FOUND. § 23.03[5] (1993).

33. *Jay County Rural Elec. Membership*, 692 N.E.2d at 910.

complaint for declaratory judgment, RUS had not yet approved the merger. In fact, RUS suspended the merger indefinitely due to concerns about the assignability of the all-requirements contracts of the cooperative's members, one of which was the subject of this lawsuit.[34] As the court noted, under section 2-610, when a party repudiates a contract anticipatorily, the other party may treat the repudiation as a breach and may seek damages, however, the repudiation "must be positive, absolute, and unconditional."[35] The court of appeals agreed with the trial court that factual questions remained as to whether the electric company had acted prematurely, whether the proposed merger was itself a repudiation, and whether the electric company simply wanted to get out of the contract for its own benefit and was using the proposed merger as a pretext.[36]

The electric company also argued, pursuant to section 2-609, that it had demanded adequate assurances of performance, either assuring that the merger discussions had ceased or that the cooperative would be able to perform.[37] The electric company claimed that the failure of the cooperative to give those assurances resulted in a breach that entitled the electric company to terminate the contract. However, according to the court, the electric company demanded for assurances filing the suit and, therefore, this case did not fall within the UCC's requirements.[38] Indeed, the court could also have stated that, contrary to the electric company's position that it had reasonable grounds for insecurity, its own lawsuit gave the cooperative reasonable grounds for insecurity as to whether the electric company would perform, thereby entitling the cooperative to demand reasonable assurances of performance under section 2-609. Further, even assuming that the electric company had a right to demand assurances of performance, both the trial court and the court of appeals agreed that the cooperative's response to the electric company's demands was likely to be found to constitute satisfactory assurance of performance.[39]

B. The Predominant Thrust Test; Course of Dealing (Section 2-105); Confirmations (Sections 2-201, 2-207); Acceptance by Performance (Section 2-206)

In *Echo, Inc. v. Whitson Co.*,[40] which involved Illinois law, the Seventh Circuit addressed numerous issues arising from the cancellation of a distributorship agreement by the seller and its refusal to deliver goods to its buyer.[41] At the outset, the court stated that because the predominant thrust of the

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34. *See id.* at 910-11.
35. *Id.* at 910.
36. *Id.* at 911.
37. *See id.*
38. *Id.*
39. *Id.*
40. 121 F.3d 1099 (7th Cir. 1997).
41. In a prior opinion, the court of appeals affirmed the district court's grant of summary judgment in favor of the seller against the buyer who had claimed that seller had breached the

hybrid distributorship agreement was the sale of goods, the UCC governed the matter in its entirety.[42] This is consistent with the Indiana Supreme Court's declaration that where the predominant thrust or aspect of a contract is the sale of goods, notwithstanding the presence of other matters, the UCC governs the contract and all matters arising under it.[43]

The primary issue in the present discussion is the buyer's contention that the seller had breached a contract to fill an order placed by the buyer pursuant to the distributorship agreement. That agreement provided, "'[a]ll orders for Products shall be subject to acceptance by [seller] at Lake Zurich, Illinois' [which was] where its headquarters were located."[44] The opinion does not mention if the individual order forms contained similar language. The buyer contended that the seller had waived the requirement of home-office approval by regularly sending its sales managers to negotiate with distributor-buyers. The court declared that the practice of sending sales managers who signed orders placed by buyers was not inconsistent with this term in that the seller's sales managers were merely soliciting offers by way of specific orders that could then be accepted at the home office.[45]

The court's position is sound. Professor Allen Farnsworth states:

> [T]he insertion into a proposal of a clause that reserves to its maker the power to close the deal is a compelling indication that the proposal is not an offer. A common example provides that the agreement is not binding until it has been approved at the home office of the maker of the proposal.[46]

Professor Farnsworth suggests that possible reasons for such a clause may be to assure that the salesman has not changed standard terms or that the credit of the buyer is good.[47]

The court continued that even if the practice of sending out sales managers were inconsistent with the distributorship agreement, it was a course of dealing pursuant to UCC section 2-105 that was "trumped" by the express distributorship agreement.[48] The characterization of the practice as a course of dealing raises

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overall distributorship agreement. Echo, Inc. v. Whitson Co., 52 F.3d 702 (7th Cir. 1995). The present decision involved the buyer's counterclaims in the seller's action for unpaid invoices.

42. *Echo*, 121 F.3d at 1102.

43. *See* Insul-Mark Midwest, Inc. v. Modern Materials, Inc., 612 N.E.2d 550, 554 (Ind. 1993). In adopting the predominant thrust test, the court resolved a conflict between districts of the court of appeals. *Compare* Baker v. Compton, 455 N.E.2d 382 (Ind. Ct. App. 1983) (predominant thrust test), *with* Data Processing Servs. Inc. v. L.H. Smith Oil Corp., 492 N.E.2d 314 (Ind. Ct. App.) (bifurcated approach so that the UCC applied only to goods issues), *reh'g denied*, 493 N.E.2d 1272 (Ind. Ct. App. 1986).

44. *Echo*, 121 F.2d at 1102.

45. *Id.*

46. 1 E. ALLEN FARNSWORTH, FARNSWORTH ON CONTRACTS § 3.10 (1990).

47. *Id.*

48. *Echo*, 121 F.3d at 1102. UCC section 1-205(1) states: "A course of dealing is a

some question, because a course of dealing is "restricted, literally, to a sequence of conduct between the parties previous to the agreement."[49] Rather, the practice seems to be more like a "course of performance" of the distributorship contract itself.[50] Although express terms of a contract will control a course of dealing or a course of performance,[51] a course of performance that varies from a requirement in the contract may constitute a waiver of that requirement.[52] However, the court specifically found that there was "no indication of waiver by [the seller,]"[53] thus negating the possibility that even if the practice in question were construed to be a course of performance, the express requirement of home office approval was not waived.

The buyer also argued that the seller actually had accepted the order when the seller sent out a letter addressed "'To All Distributors,' . . . 'recapping'" the Spring 1993 orders, and requesting distributors to verify that the data with respect to new orders was correct.[54] The court refused to find that the letter was "an objective manifestation of acceptance that could create a contract."[55] Rather than act as a commitment to supply the goods ordered, the letter served verification and clarification purposes only.[56] The letter at most acknowledged receipt of the orders, and did not constitute acceptance of any buyer's order.[57]

As a further argument, the buyer contended that if the letter was not an acceptance of its offer in traditional offer-acceptance terms, it "operate[d] as an acceptance" because it was a "confirmation" within the meaning of section 2-207(1).[58] The court quickly rejected this argument by observing that the confirmation to which that section refers is a written confirmation of a prior oral agreement. The purpose of the written confirmation is to satisfy the statute of frauds found in section 2-201.[59] As the court noted: "To quote one UCC

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sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct." U.C.C. § 1-205(1).

49. U.C.C. § 1-205, cmt. 2.

50. UCC section 2-208(1) states: "Where the contract for sale involves repeated occasions for performance . . . and opportunity for objection to it by the other, any course of performance accepted or acquiesced in . . . shall be relevant to determine the meaning of the agreement." *Id.* § 2-208(1).

51. *See id.* §§ 1-205(4), 2-208(2).

52. *See id.* § 2-208(3).

53. *Echo*, 121 F.3d at 1102.

54. *Id.* at 1101 (quoting Letter from Echo, Inc., to Power Tool Co. (Oct. 15, 1992)).

55. *Id.* at 1103.

56. *See id.*

57. *See id.*

58. *See id.* UCC section 2-207(1) states: "A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon . . . ." U.C.C. § 2-207(1).

59. *See Echo*, 121 F.3d at 1103-04.

commentator, 'A confirmation differs from an acceptance in that if it is a true confirmation, a contract between the parties already exists.'"[60] Here, there was no prior agreement for the "recap" letter to confirm.[61] The seller never accepted the buyer's offer to buy, and judgment for the seller on the buyer's counterclaim was appropriate.

C. Non-recoverability of Fees as Incidental or Consequential Damages (Section 2-715)

In *Indiana Glass Co. v. Indiana Michigan Power Co.*,[62] the Indiana Court of Appeals joined "the overwhelming weight of authority from other jurisdictions indicating that attorney's fees are not recoverable under [section] 2-715."[63] A glass manufacturer sued a power company for negligence and breach of the UCC implied warranties of merchantability[64] and fitness for a particular purpose[65] following damage to the manufacturer's production caused by the power company's failure to supply electricity of consistent voltage. After the trial court ruled that a sale of electricity is a sale of goods within the scope of the UCC and that the power company had failed to disclaim the UCC warranties, the parties settled all issues between them except the issue of attorney's fees.[66] The successful buyer claimed that it could recover its attorney's fees as incidental or consequential damages under section 2-715. Although this was a novel issue in Indiana law, the court had previously decided the issue under Kentucky's version of section 2-715, which is identical to that of Indiana.[67]

The buyer urged the court to ignore the majority rule and hold that attorney's fees are recoverable either as incidental or consequential damages under section 2-715 or under general principles of law and equity, which, according to section 1-103, have not been displaced by the UCC. The court properly rejected these arguments. The incidental damages provided for in section 2-715(1) are expenses incurred by a rejecting or revoking buyer in handling the goods or in effecting cover.[68] The consequential damages in section 2-715(2)(a), described as "any loss," were not meant to change the general rule of law that each party must bear its own legal expenses.[69]

The buyer also contended that section 1-106(1), which states that UCC

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60. *Id.* at 1103 (quoting HAROLD GREENBERG, RIGHTS AND REMEDIES UNDER U.C.C. ARTICLE 2 § 7.11 (1987)).

61. *See id.* at 1104.

62. 692 N.E.2d 886 (Ind. Ct. App. 1998).

63. *Id.* at 888.

64. U.C.C. § 2-314.

65. *Id.* § 2-315.

66. *See Indiana Glass*, 692 N.E.2d at 887.

67. *See* Landmark Motors v. Chrysler Credit Corp., 662 N.E.2d 971, 976-77 (Ind. Ct. App. 1996).

68. *See Indiana Glass*, 692 N.E.2d at 888.

69. *See id.* at 888-89.

remedies "'shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed,'" justified an award of its attorney's fees.[70] The court responded that section 1-103 preserves applicability of the principles of law and equity, including the law merchant, unless "explicitly displaced by the provisions" of the UCC.[71] The court also held that section 2-715 does not displace the common law rule in Indiana that precludes recovery of attorney's fees in the absence of a specific statute.[72]

The court could have pointed to the single instance in Indiana's version of the UCC that expressly provides for recovery of attorney's fees. The Official Draft's version of section 2-721 provides that all UCC remedies shall be available in actions based on fraud or material misrepresentation.[73] Indiana Code section 26-1-2-721 adds a unique provision, not found in the UCC of any other state, that a successful plaintiff in such a suit "shall also be entitled to recover reasonable attorney's fees."[74] The Indiana General Assembly knew how to change the general rule that each party must bear its own legal costs, and did so in this one section. The failure to so provide in other sections of the Indiana Code indicates that it intended no other changes in the prevailing rule.

D. Modification and Waiver (Section 2-209); The Parol Evidence Rule (Section 2-202); The Statute of Frauds (Section 2-201); and Requirements Contracts (Section 2-306)

The dispute in *Pepsi-Cola Co. v. Steak 'N Shake, Inc.*,[75] arose from claims and counterclaims of breach of a contract pursuant to which the buyer agreed to replace its then current soft drink products with the seller's products. Following months of negotiation, the seller sent to the buyer a proposed draft agreement together with an unsigned letter (the "Letter") from one of seller's vice-presidents who described the seller's marketing programs in somewhat more detail than contained in the draft agreement.[76] Further drafts were exchanged, with the "Contract" finally consisting of two signed agreement forms. The Contract contained a merger or integration clause, a no-oral-modification clause, as well as a marketing provision that described the parties' participation in the Contract.[77]

Shortly thereafter, the buyer sent a letter requesting that the seller send a signed copy of the Letter and that the Letter be made part of the Contract.[78] The

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70. *Id.* at 889 (quoting U.C.C. § 1-106(1)).
71. *Id.*
72. *Id.*
73. U.C.C. § 2-721.
74. IND. CODE § 26-1-2-721 (1998).
75. 981 F. Supp. 1149 (S.D. Ind. 1997).
76. *See id.* at 1152.
77. *See id.*
78. *See id.*

seller sent the signed copy but did nothing else. The buyer then sent a second letter that purportedly summarized a telephone agreement to incorporate the Letter into the Contract and requested a signed confirmation of that oral agreement to incorporate the Letter.[79] The seller did not reply. The buyer again sent a letter demanding incorporation of the Letter into the Contract and stated that if the seller did not comply with this demand, the buyer would assume that the seller will stand behind the terms of the Letter and that it will be part of the Contract. Again, the seller did not respond.[80]

Three years later, the buyer gave notice of termination, the seller sued for breach, and the buyer counterclaimed that it was terminating for cause in that the seller itself had breached. Both parties moved for summary judgment on various issues, and the court denied all of these motions.[81]

The first issue before the appellate court was whether the Letter was part of the Contract. Citing section 2-209(2), the *Pepsi-Cola* court observed that although any contract may be modified by subsequent agreement of the parties, the UCC permits the parties to agree not to modify the agreement between them except by a signed writing, which the parties did in this case.[82] The record was clear that the seller never agreed to the modification.

The buyer also contended that the seller's failure to respond to the buyer's last letter—the one saying that in the absence of a reply the buyer would assume the Letter to be part of the Contract—was a waiver of the no-oral-modification clause and that the Contract should be deemed modified to include the Letter.[83] The court stated that although section 2-209(4) allows an unsuccessful modification under section 2-209(2) to operate as a waiver of the no-oral-modification requirement, a party must rely on the attempted modification and the reliance must be reasonable.[84] In this instance, the buyer may have relied, but its reliance was unreasonable in view of the seller's repeated refusals by "'loud silence'" to incorporate the Letter into the Contract.[85] Furthermore, a waiver can arise from a party's silence only where that party has a duty to speak, a duty that the buyer could not establish in this case, and a duty the court was unwilling to impose on the seller.

The second issue the court addressed was whether the Letter was admissible as evidence of the Contract's meaning with respect to the marketing provision, an issue that implicated section 2-202, the UCC's parol evidence rule.[86] The rule

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79. *See id.*

80. *See id.*

81. *See id.* at 1151.

82. *Id.* at 1154.

83. *See id.* at 1155.

84. *Id.*

85. *Id.*

86. UCC section 2-202 states:

> Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted

itself determines what prior or contemporaneous agreements or terms are part of the written agreement at issue. The interpretation of an ambiguous term in that agreement may be considered an exception to the rule.[87] Indeed, if the issue is one of interpretation, some scholars state that the parol evidence rule does not apply at all.[88]

The court clearly and correctly stated: "While parol evidence may not be introduced to add to or contradict a fully integrated written agreement, evidence outside the document may be introduced to clarify or interpret an ambiguous term or phrase."[89] The court next reiterated the traditional definition of "ambiguity," that "[a] contract term is ambiguous if a reasonable person could find that it is susceptible to more than one interpretation,"[90] and concluded that because the "marketing program," as used in the Contract was susceptible to several interpretations, the Letter was admissible to explain the term.[91]

The final UCC argument the buyer raised in *Pepsi-Cola* was that the Contract failed to comply with the Statute of Frauds and therefore, was unenforceable because it lacked a quantity term. The court rejected this argument as well and stated: "A writing, which contemplates a requirements contract, satisfies the Statute of Frauds even though the writing does not detail any specific quantities."[92] The court's position is sound and is in accord with current thinking.[93] The court concluded that a reasonable jury could find that the contract was a requirements contract, particularly because it provided for payments to the buyer's former soft drink supplier thereby making the seller its only supplier, and that the buyer was required to have four of the seller's products available at each of its restaurants.[94] The court did not, however, rule explicitly that this was a requirements contract, only ruling that the language satisfied the Statute of Frauds, because the issue of whether the Contract was a requirements contract was a question of fact for the fact finder.[95]

> by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented . . . .
>
> (b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.

U.C.C. § 2-202.

87. *See* DOUGLAS J. WHALEY, CASES, MATERIALS AND PROBLEMS ON CONTRACTS 561, 598 (2d ed. 1993).

88. *See, e.g.*, JOHN E. MURRAY, JR., MURRAY ON CONTRACTS § 85A (3d ed. 1990).

89. *Pepsi-Cola*, 981 F. Supp. at 1156.

90. *Id.* (citing Canada Dry Corp. v. Nehi Bev. Co. of Indianapolis, 723 F.2d 512, 519 (7th Cir. 1983); Piskorowsi v. Shell Oil Co., 403 N.E.2d 838, 844 (Ind. Ct. App. 1980)).

91. *Id.* at 1157.

92. *Id.* at 1158 (citing Zayre Corp. v. S.M. & R. Co., 882 F.2d 1145, 1154 (7th Cir. 1989)). The UCC specifically authorizes requirements contracts. U.C.C. § 2-306.

93. See GREENBERG, *supra* note 60, § 8.5 and the cases cited therein; 1 WHITE & SUMMERS, *supra* note 13, § 2-4 n.12.

94. *Pepsi-Cola*, 981 F. Supp. at 1158-59.

95. *Id.* at 1159.

E. Change of Requirements Under a Requirements Contract (Section 2-306)

Indiana-American Water Co. v. Town of Seelyville[96] also involved a long-term requirements contract, this time for a supply of water. In 1983, the water company agreed to sell and the town agreed to buy through 2008, "such quantities of water as the Town may hereafter from time to time need."[97] Long before the parties entered into the contract, the town had purchased land that could be used as a well field for the supply of water.[98] In 1997, when the town announced it would sell bonds to finance the construction of its own water supply on that well field, the water company sought a declaratory judgment that the town's plan would result in a breach of the supply contract.[99]

The court of appeals considered two issues: First, whether the contract was a requirements contract, authorized by UCC section 2-306, or merely an indefinite quantities contract that was illusory because it imposed no obligation on the parties; and, second, whether the planned reduction in the town's requirements under the contract was in good faith, as authorized by section 2-306, or in bad faith, thereby constituting a breach of contract.[100]

The court had relatively little difficulty in agreeing with the trial court that the contract in this case constituted an enforceable requirements contract "in which the purchaser agrees to buy all of its needs of a specified material exclusively from a particular supplier, and the supplier agrees, in turn, to fill all of the purchaser's needs during the period of the contract."[101] The more difficult issue for the court was whether the town/buyer was acting in good faith in determining its requirements, as mandated by section 2-306(1).[102]

The court correctly observed that the seller assumes the risk that the buyer's requirements may change, but "the buyer is not free, on any whim, to quit buying from seller."[103] The essential test of the buyer's good faith in changing its requirements is whether the buyer has legitimate business reasons for doing so or is merely attempting to get out of a disadvantageous contract.[104] The court concluded that the "Town's decision to develop its preexisting well field

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96. 698 N.E.2d 1255 (Ind. Ct. App. 1998).
97. *Id.* at 1257.
98. *See id.*
99. *See id.* at 1257-58.
100. *Id.* at 1257.
101. *Id.* at 1259.
102. As applicable to this case, UCC section 2-306(1) states:

> A term which measures the quantity by . . . the requirements of the buyer means such actual . . . requirements as may occur in good faith, except that no quantity unreasonably disproportionate to any stated estimate or in the absence of a stated estimate to any normal or otherwise comparable prior . . . requirements may be . . . demanded.

U.C.C. § 2-306(1).
103. *Indiana-American Water*, 698 N.E.2d at 1260.
104. *See id.* at 1261.

constitutes a legitimate, long-term business decision, and not merely a desire to avoid the terms of its contract with [the] Water Company."[105]

II. ARTICLES 3 & 4—NEGOTIABLE INSTRUMENTS AND BANK COLLECTIONS: STATUTE OF LIMITATIONS FOR CONVERSION OF CHECKS

Contrary to the vast majority of jurisdictions, the Indiana Court of Appeals, in *UNR-Rohn, Inc. v. Summit Bank*,[106] ruled that a cause of action for conversion of a check under former section 3-419[107] accrues when the aggrieved party "could have, in the exercise of ordinary diligence, discovered the conversion of the checks."[108] The plaintiff alleged that the bank, in which it had several accounts, had converted checks payable to plaintiff by cashing them or depositing them into the personal account of one of plaintiff's employees until 1991, when the plaintiff discovered the embezzlement.[109] The bank contended that the two-year statute of limitations relating to personal property barred claims for conversion of any checks cashed or negotiated prior to 1991, because the prior version of Article 3 did not contain an applicable statute of limitations.[110]

Although it specifically "recognize[d] that the vast majority of authority from other jurisdictions runs against applying the discovery rule to an action for conversion of negotiable instruments under UCC section 3-419 in the absence of fraudulent concealment on the part of the defendant asserting the defense of the statute of limitations,"[111] the court rejected the discovery rule as being contrary to the policy of Indiana.

The court analyzed the history of the so-called discovery rule as it applies to tort actions in general and expressly refused "to carve out an exception to the discovery rule in injuries to personal property involving conversion of negotiable instruments [as being] wholly incongruous and inconsistent with Indiana's system of jurisprudence."[112] Accordingly, the court reversed the grant of summary judgment in favor of the bank on this issue and remanded for a factual finding with respect to the date when the bank's customer could have discovered the conversions.[113]

This result will continue to apply under the revised version of Article 3, which states that an action for conversion of a negotiable instrument "must be commenced within three years after the cause of action accrues."[114] The official

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105. *Id.*
106. 687 N.E.2d 235 (Ind. Ct. App. 1997).
107. IND. CODE § 26-1-3-419 (1993) (recodified as amended at IND. CODE § 26-1-3.1-420 (1998)).
108. *UNR-Rohn*, 687 N.E.2d at 241.
109. *See id.* at 236.
110. *See id.* at 239-40.
111. *Id.* at 241 n.5.
112. *Id.* at 241.
113. *Id.*
114. IND. CODE § 26-1-3.1-118(g) (1998).

comment thereto states that the section "does not define when a cause of action accrues."[115] Thus, Indiana will continue to have a rule under the UCC that is not "uniform."

In most cases of employee embezzlement, a diligent employer, acting with due care, should be able to discover the employee's defalcations before the statute of limitations runs. Moreover, the UCC's policy is that employers should bear the risk of hiring dishonest employees, and banks will be liable only on a comparative negligence basis.[116] If the employer in *UNR-Rohn* entrusted the dishonest employee with responsibility for checks, the forged endorsements would have been effective, and the employer would have no recovery against the bank for conversion unless the bank's failure to exercise ordinary care contributed to the loss.[117]

III. ARTICLE 8—INVESTMENT SECURITIES

The question in *Giuffre Organisation, Ltd. v. Euromotorsport Racing, Inc.*,[118] was whether a share of stock in Championship Auto Racing Teams, Inc. ("CART") was an investment security within Article 8 of Indiana's UCC, so that a security interest under Article 9 could be perfected by possession alone.[119] Applying Indiana law, the Seventh Circuit Court of Appeals affirmed the U.S. District Court for the Southern District of Indiana decision that it was not an investment security within Article 8.

Euromotorsport owned two shares of stock in CART, which gave it both a financial interest and membership in CART, as well as the right and obligation to participate in CART races.[120] When various problems led to financial difficulties, Euromotorsport entered into a complex financial relationship with Giuffre and gave one CART share to Giuffre as security for its financial support. Unfortunately, creditors filed an involuntary petition in bankruptcy against Euromotorsport, and CART redeemed the two shares for failure to participate in its races in violation of Euromotorsport's membership obligation.[121] Giuffre requested that it be treated as a secured creditor of the stock certificate that it had possessed thereby giving it entitlement to the cash paid to redeem it.[122] Giuffre claimed that the CART share was a "certificated security" within section 8-102 of the 1977 version of Article 8,[123] and that its security interest was perfected by

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115. *Id.* cmt. 1.
116. *See* IND. CODE § 26-1-3.1-405(b) (1998).
117. *See id.*
118. 141 F.3d 1216 (7th Cir. 1998).
119. *Id.* at 1217. *See also* U.C.C. § 9-115 & cmt. 2.
120. *See Giuffre Organisation*, 141 F.3d at 1216.
121. *See id.* at 1217.
122. *See id.*
123. IND. CODE § 26-1-8-102 (1993) (recodified as amended at IND. CODE § 26-1-8.1-102 (1998)).

possession.[124] The bankruptcy judge agreed, but the district court did not.

On appeal, the district court ruled that the restrictions on CART stock precluded the stock from being certificated securities within Article 8, and only a security agreement under section 9-203 plus a filed financing statement under section 9-302 could accomplish perfection.[125] Accordingly, Giuffre was merely an unsecured creditor. The court of appeals affirmed.

One key issue the Seventh Circuit had to resolve, without guidance from any Indiana decision on point, was whether a share in a closely held corporation was a certificated security within Article 8, possession of which perfects a security interest under Article 9. Former section 8-102(1)(ii) defines such a security as being "'of a type commonly dealt with on securities exchanges or commonly recognized in any area in which it is issued or dealt in as a medium for investment.'"[126] In 1985, the Supreme Court of the United States held that sale of stock in a closely held business was a sale of a security under federal law.[127] Revised Article 8 incorporates the Supreme Court's decision into UCC sections 8.1-102(a)(15)(iii)(B) and 8.1-103(a). The *Giuffre Organisation* court concluded that, in view of the *Landreth* decision plus the swift enactment of revised Article 8 in Indiana, the Indiana Supreme Court would hold as many other courts have: Stock in closely held corporations can be certificated securities within the earlier version of Article 8.[128]

However, the CART stock was not simply a share in a closely held corporation.[129] As described by the court:

> A share of stock in CART represents not only an investment (and an opportunity to share in whatever profits CART makes) but also a membership, and thus a right to participate in the races. No owner can enter a car without the membership that is linked to ownership of CART stock. Ability to pay for a share is not enough to buy one . . . . Transfer of any CART share requires the approval of CART's board, which may be had only if CART determines that the buyer is fit to race.[130]

Moreover, ownership of the shares carried with it not only an interest in the corporation but also a contractual obligation to race.[131] Euromotorsport's failure to race breached that obligation and resulted in the redemption of the two shares pursuant to the terms of that obligation. Thus, CART shares were more like an interest in a franchise operation or ownership of a cooperative apartment, neither

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124. *See Giuffre Organisation*, 141 F.3d at 1217.

125. *See id.*

126. *Id.* at 1217 (quoting U.C.C. § 8-102(1)(ii), *found in* IND. CODE § 26-1-8-102(1)(a)(ii) (1993) (recodified as amended at IND. CODE §§ 26-1-8.1-102(4), (15) (1998))).

127. Landreth Timber Co. v. Landreth, 471 U.S. 681, 697 (1985).

128. *Giuffre Organisation*, 141 F.3d at 1218.

129. *Id.*

130. *Id.* at 1216.

131. *See id.*

of which is a certificated security, notwithstanding the label affixed to it.[132]

In affirming the determination of the district court, the court of appeals concluded:

> In diversity litigation under *Erie*[133] all we can do is predict how the state courts will handle the subject when it arrives. Perhaps the Supreme Court of Indiana will never have an opportunity to interpret the definition of a security in the 1977 version of Article 8, but we are reasonably confident that if it did so it would treat a document used to control participation in a professional sport as a "franchise" or something similar rather than as a "security."[134]

IV. ARTICLE 9—SECURED TRANSACTIONS: REPOSSESSION AND BREACH OF THE PEACE (SECTION 9-503)

Birrell v. Indiana Auto Sales & Repair[135] presented a novel question for Indiana courts. In that case an independent contractor, paid by an automobile dealer/creditor to repossess an automobile, directed a fifteen-year-old boy who had no driver's license to make the repossession.[136] The boy did so, drove above the speed limit, and crashed into plaintiff's car. Plaintiff filed suit against the creditor and the repossession contractor to recover for her personal injuries.[137] The trial court granted summary judgment for the dealer and the plaintiff appealed.[138]

The UCC issue in this appeal was whether the repossession violated the statutory duty imposed by section 9-503 that permits repossession without judicial process "if this can be done without breach of the peace."[139] If it did, the automobile dealer could be liable for the repossessor's negligence, an exception to the general rule that an employer is not responsible for the negligence of an independent contractor.[140]

The court noted that the UCC does not define the term "breach of the peace." According to White and Summers, the term is a "well-worn phrase," not redefined by the UCC drafters, and "has been the subject of countless judicial opinions."[141] In ruling that the boy's conduct did not constitute a breach of the peace within section 9-503, the *Birrell* court relied on two non-Indiana cases, both of which support the rule that traffic violations following the actual taking

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132. *See id.* at 1218-19.
133. Erie R.R. v. Tompkins, 304 U.S. 64 (1938).
134. *Giuffre Organisation*, at 1219.
135. 698 N.E.2d 6 (Ind. Ct. App. 1998).
136. *Id.* at 7.
137. *See id.*
138. *See id.*
139. *Id.* at 8.
140. *See id.* at 7-8.
141. 4 WHITE & SUMMERS, *supra* note 13, § 34-7.

of the car do not violate section 9-503.[142] Whether the boy's conduct after the repossession might constitute a separate breach of the peace is irrelevant. The UCC deals only with conduct during the actual repossession, not thereafter. As the act of repossession moves away from the residence of the debtor, the likelihood of a breach of the peace within the UCC diminishes substantially.[143] It would seem rather plain that once the repossession itself is achieved peacefully, the subsequent action of the repossessor is irrelevant to this section of the UCC, even if that action is itself a breach of the peace.

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142. *Birrell*, 698 N.E.2d at 8-9 (discussing Wallace v. Chrysler Credit Corp., 743 F. Supp. 1228 (W.D. Va. 1990); Jordan v. Citizens & South Nat'l Bank, 298 S.E.2d 213 (S.C. 1982)).

143. *See* WHITE & SUMMERS, *supra* note 13, § 34-7.

RECENT DEVELOPMENTS IN WORKER'S COMPENSATION LAW

CAROL MODESITT WYATT*

INTRODUCTION

The Worker's Compensation Act (the "Act")[1] is a compromise between employers and employees. The Act allows an injured worker to recover a percentage of his average weekly wage during disability, compensation for any permanent loss of function, and where the injury is fatal, benefits paid directly to the employee's dependents. The Act also provides for the payment of reasonable medical expenses. At the same time, the Act shields employers from conventional tort liability. This Article surveys the developments in Indiana's Worker's Compensation law between October 1997 and October 1998 and reviews a wide variety of cases and issues affecting Indiana practitioners. Recent cases have addressed such issues as the employee's receipt of temporary total disability, permanent total disability, employer liens, intentional injuries, and the election of remedies. In addition, the 1996 legislative session brought about many significant statutory changes that took effect in 1997.

I. TEMPORARY TOTAL DISABILITY PRECLUDED

Temporary total disability ("TTD") is the payment of benefits during the time when the employee is temporarily unable to engage in his regular job duties.[2] In *Ballard v. Book Heating & Cooling*,[3] the court determined that the employee's receipt of unemployment compensation precluded him from receiving TTD for the same period of time.[4]

In *Ballard*, the employee suffered a compensable injury to his back in August 1995. The employee was later terminated from Book Heating in February 1996. He applied for and began receiving unemployment compensation in March 1996. On March 5, 1996, the employee was placed on medical leave and remained unable to work per doctor's order until August 1996, when he reached the maximum medical improvement ("MMI").[5] The employee requested that the employer pay TTD benefits from August 1995 to August 1996. The employer argued that it should not be required to pay TTD during the time period wherein

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* Associate, Locke Reynolds Boyd & Weisell. B.A., 1994, Butler University; J.D., 1998, Indiana University School of Law—Indianapolis. Special thanks to Sybil Richard for assisting in the research and drafting of this Article.

1. IND. CODE §§ 22-3-1-1 to -3 (1998).

2. *See id.* § 22-3-3-8. TTD is payable at the rate of sixty-six and two-thirds percent of the employee's average weekly wage, not to exceed the statutory maximum in effect at the time of the employee's accident. *See id.*

3. 696 N.E.2d 55 (Ind. Ct. App. 1998).

4. *Id.* at 59.

5. *See id.* at 56.

the employee received unemployment compensation.[6]

Recognizing that this presented an issue of first impression, the Indiana Court of Appeals reviewed opinions from other jurisdictions. The review revealed a split of authority on the issue of whether the receipt of either worker's compensation or unemployment benefits precluded an entitlement to the other.[7] Focusing on the instant case, the court noted that the purpose of TTD benefits is to compensate the employee for lost earning power due to disability. During the time the employee undergoes treatment, it is relevant whether the employee has the ability to return to work of the same kind or character.[8] If the employee does not have the ability to return to work of the same kind or character, then the employee is temporarily totally disabled and may be entitled to TTD benefits.[9] In contrast, the court noted that one may receive unemployment benefits only if one is physically and mentally able to work, available for work, and making an effort to obtain work.[10]

The employee in *Ballard* represented to the Unemployment Insurance Division in March 1996 that he was ready, willing, and able to return to work.[11] At the same time, the employee represented to the Worker's Compensation Board that he was temporarily totally disabled and unable to return to work.[12] The court held that "[a]lthough our statutes do not expressly prohibit a claimant from receiving both types of benefits, we conclude that our legislature could not have intended for an employee to recover dual benefits under these circumstances."[13] Accordingly, the employee was precluded from receiving TTD benefits for the same period of time that he received unemployment benefits.

The court recognized that some jurisdictions considering this issue offset the amount of worker's compensation benefits with the amount of unemployment benefits received;[14] however, the court did not engage in such a discussion with regard to Indiana law. Thus, the court took an all or nothing approach. Essentially, practitioners should be aware that if their employee client receives unemployment benefits, such receipt will preclude the award of TTD benefits. Likewise, practitioners representing employers should investigate the possibility that the employee applied for or received unemployment benefits. Presumably, even if the employee merely applied for unemployment benefits without

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6. *See id.*

7. *See id.* at 57. The court noted that some states allow recovery of both worker's compensation and unemployment benefits while other states either denied or reduced the amount of worker's compensation benefits by the amount of unemployment benefits received, or vice-versa. *Id.*

8. *See id.* (citing Covarubias v. Decatur Casting, 358 N.E.2d 174, 176 (Ind. Ct. App. 1976)).

9. *See id.*; *see also* IND. CODE § 22-3-3-8 (1998).

10. *Ballard*, 696 N.E.2d at 57 (citing IND. CODE § 22-4-14-3 (1998)).

11. *Id.*

12. *See id.* at 57-58.

13. *Id.* at 58.

14. *Id.* at 57.

receiving such benefits, the employee would still be precluded from receiving TTD benefits. To find otherwise would appear to be contrary to the court's reasoning in *Ballard*.[15]

II. "REASONABLE EMPLOYMENT" IN THE CONTEXT OF A PERMANENT TOTAL DISABILITY CLAIM DEFINED

Permanent total disability ("PTD") is the payment of benefits after the employee's injury has become quiescent and the employee is deemed permanently unable to engage in any reasonable employment.[16] The Act does not define what constitutes "reasonable employment;" however, the Indiana Supreme Court recently addressed the meaning of this term.

In *Walker v. Indiana*,[17] the employee sustained a back injury while at work and, after undergoing surgery, had a twenty-five percent permanent partial impairment ("PPI").[18] Following the surgery, the employee was unable to return to her previous position. She claimed she was unable to return to any reasonable employment and was entitled to PTD benefits.[19] Her employer offered her a highly accommodated, but temporary position as a seamstress under the State's partial disability program, contending that such employment constituted "reasonable employment," precluding the receipt of PTD benefits.[20] The employee declined the tendered employment and pursued a PTD claim.

The Indiana Supreme Court held that the tendered employment was not "reasonable employment," stating two reasons in support of its holding.[21] First, the court noted that "the temporary nature of the employment is in itself sufficient reason to conclude that it cannot constitute reasonable employment such that it defeats a claim of total permanent disability."[22] Second, and more importantly, the court held that "work that is highly accommodated to suit the needs and disabilities of a particular claimant cannot defeat a claim of total permanent disability where it is clear that the claimant could not find similar work under normally prevailing market conditions."[23]

While in practice an employer may still be able to defeat a PTD claim by

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15. The court stated that "[t]o suggest that one who was physically and mentally able to work, available for work, and was making an effort to secure full-time work was at the same time totally disabled, would be contrary to law." *Id.* at 58.

16. *See* IND. CODE § 22-3-3-10 (1998).

17. 694 N.E.2d 258 (Ind. 1998).

18. *Id.* at 263. PPI benefits are payable after the injury is quiescent and the permanent loss of a physical function has been medically assessed. The PPI rating is a rating by degrees assigned to represent the employee's permanent loss of function. Compensation of that loss is determined by the scheduled rate that corresponds to the given PPI rating. *See* IND. CODE § 22-3-3-10 (1998).

19. *See Walker*, 694 N.E.2d at 264.

20. *See id.*

21. *Id.* at 267.

22. *Id.*

23. *Id.*

showing that it tendered reasonable employment, the employer must now be prepared to establish that such tendered employment is similar to that employment generally available in the competitive labor market. Further, *Walker* makes it clear that an employee is not required to accept make-work or a highly accommodated job. The employee may, instead, pursue a PTD claim.

In addition, the court in *Walker* stated that after the employee establishes disability or impairment, education, work history and age, and establishes that attempts to find suitable employment have been unsuccessful, then the burden of proving that reasonable employment exists shifts to the employer.[24] The court stated:

> Shifting the burden of production to the employer under these circumstances is justified because it is much easier for the employer, by virtue of its contact with the labor market, to prove the claimant's employability than it is for the employee to attempt to prove the universal negative of being totally unemployable.[25]

Essentially, after the employee has proved his limitations and his failed attempts to find employment, he does not then need to prove that no reasonable employment exists. The employer must produce evidence that reasonable employment in fact exists. As a practical matter, the employer likely will have to retain a qualified vocational expert witness to accomplish this task.

III. Employer Liens

The Act provides that if an employee's injury or death is caused by someone other than the employer or a co-employee, the injured employee or the employer may maintain a civil action against that party.[26] If the employee recovers from a third party, then the employer may receive reimbursement for the amount of compensation benefits and medical expenses paid on behalf of the employee and, accordingly, the employer is no longer responsible for the payment of benefits.[27] However, the employer must pay a pro-rata share of litigation costs and expenses and must also pay a statutory fee to the employee's attorney.[28] This later provision has sparked much controversy over the past year.

In particular, practitioners eagerly await the Indiana Supreme Court's decision in *Spangler, Jennings & Daugherty P.C. v. Indiana Insurance Co.*[29] In 1997, the Indiana Court of Appeals held that the worker's compensation carrier must contribute a pro-rata share of attorneys fees on the entire amount of future

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24. *Id.* at 265-66 (citations omitted).

25. *Id.* at 266 (citing E.R. Moore Co. v. Industrial Comm'n, 376 N.E.2d 206, 210 (Ill. 1978)).

26. *See* Ind. Code § 22-3-2-13 (1998).

27. *See id.*

28. *See id.*

29. 685 N.E.2d 705 (Ind. Ct. App. 1997), *trans. granted*, 698 N.E.2d 1195 (Ind. 1998).

benefits it would have paid if not for the third-party recovery.[30] The *Spangler* decision was appealed to the Supreme Court of Indiana and the supreme court granted transfer. According to the Act, the lien amount may be diminished by the percentage of the employee's comparative fault.[31] Thus, under *Spangler,* the employer or worker's compensation carrier may be obligated to pay a sizeable amount of attorney's fee to the employee's attorney and such fee could exceed the amount of the lien altogether. Accordingly, practitioners await the Indiana Supreme Court's decision as it will likely impact the way practitioners view a case where a third party recovery is contemplated.

The Indiana Court of Appeals addressed liens in a different context in *Walkup v. Wabash National Corp.*[32] In *Walker,* an employee was injured while driving in the course and scope of his employment. He was injured when struck by Pruett, an uninsured motorist. The employer, who was self-insured, paid worker's compensation benefits directly to the employee in the amount of nearly $8600. The employee filed a personal injury suit against Pruett and, in November 1994, the employer placed a lien against any recovery he might receive from Pruett pursuant to section 22-3-2-13 of the Indiana Code.[33] The employee also sought recovery from Cincinnati Insurance Company under the employer's uninsured motorist coverage. In 1995, the employee received $18,000 in general damages under the employer's uninsured motorist coverage. The employer requested reimbursement pursuant to its lien and the employee refused.[34]

The employee argued that the employer was not entitled to a lien on the settlement because the settlement did not come from Pruett, the third-party tortfeasor. The employer contended that it was entitled to such funds because they were paid on behalf of the third-party tortfeasor.[35] The court held that "an award from an uninsured motorist policy paid on behalf of the third party uninsured driver is an award 'out of which the employee might be compensated from the third party.'"[36] Thus, the employer's lien was valid under the Act.

The Indiana Supreme Court reversed the court of appeals but, in doing so, agreed that an award from an uninsured motorist policy paid on behalf of the third-party tortfeasor is subject to the employer's lien.[37] Specifically, the court noted that "'an employer or worker's compensation carrier is entitled to a lien on [the] proceeds' of 'payments made to an injured employee under a[n

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30. *Id.* at 707.

31. This is true even though the amount of benefits received by the employee may not be diminished by the employee's comparative fault. Comparative fault is not an available defense under the Act.

32. 691 N.E.2d 1282 (Ind. Ct. App. 1998), *rev'd,* 702 N.E.2d 713 (Ind. 1998) (discussed below).

33. *Id.* at 1283.

34. *Id.*

35. *Id.* at 1284.

36. *Id.* (quoting IND. CODE § 22-3-2-13 (1998)).

37. Walkup v. Wabash Nat'l Corp. 702 N.E.2d 713, 714-15 (Ind. 1998).

underinsured motorist] policy.'"[38]

However, the court reversed based on the specific language of the underinsured motorist policy.[39] The policy in question excluded coverage for injuries subject to worker's compensation benefits subject to a lien by the payor of the worker's compensation benefits. Thus, the court concluded that the $18,000 paid by Cincinnati represented recovery for pain and suffering, a benefit not provided for in the Worker's Compensation Act.[40] Accordingly, because of the specific policy language, Walkup's payment from Cincinnati was not subject to Wabash's statutory lien under section 22-3-2-13 of the Indiana Code.

IV. Exclusive Remedy Provision

A. Agee v. Central Soya Co.

The Act provides compensation to the employee for injuries by accident that arise out of and in the course of the employment. The exclusive remedy provision provides that "[t]he rights and remedies granted to an employee subject to [Indiana Code section] 22-3-2 through [Indiana Code section] 22-3-6 . . . shall exclude all other rights and remedies of such employee . . . at common law or otherwise . . . ."[41] During the survey period, employees continued to challenge the exclusive remedy provision in several ways.

In *Agee v. Central Soya Co.*,[42] an employee was injured during an explosion at Central Soya's soybean processing plant. The employee filed a complaint in state court alleging that Central Soya engaged in knowing and intentional conduct, thereby removing his claim from the preview of the Act.[43] Central Soya moved to dismiss based on the exclusive remedy provision of the Act. The court stated that "[t]he dispositive issue here, is whether . . . Central Soya had actual knowledge that an injury was certain to occur."[44] The court considered all of the evidence presented and determined that the evidence fell short of establishing that Central Soya had actual knowledge that an injury was certain to occur.[45] The court stated:

> we do not believe that Central Soya's ignorance of the possibility of an explosion at its plant . . . bring[s] this case within the 'intentional injury' exception of the Act. While the evidence . . . might reveal conduct amounting to gross negligence or even recklessness on the part of Central Soya, it does not establish actual knowledge on Central Soya's

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38. *Id.* at 714 (quoting Ansert Mechanical Contractors, Inc. v. Ansert, 690 N.E.2d 305, 310 (Ind. Ct. App. 1997)).

39. *Id.* at 715-16.

40. *Id.* at 716.

41. IND. CODE § 22-3-2-6 (1998).

42. 695 N.E.2d 624 (Ind. Ct. App. 1998).

43. *See id.* at 625.

44. *Id.* at 626.

45. *Id.* at 627.

part that an injury was certain to occur.[46]

It remains difficult for an employee to establish that his injury was intentional because gross negligence and recklessness do not rise to the level of an intentional act. As the *Agee* opinion reinforces, the employee must establish that the employer had actual knowledge that an injury was certain to occur. However, employers should take steps to prevent repeated injuries to employees due to similar events or circumstances. An injury that occurs once may be an accident, but injuries that occur repeatedly may rise to the level of actual knowledge that an injury is certain to occur.

B. Walters v. Modern Aluminum

In *Walters v. Modern Aluminum*,[47] Kelly Services and Modern Aluminum were parties to a contract wherein Kelly Services provided temporary workers to Modern Aluminum. Pursuant to the contract, Kelly Services assigned Walters to render services to Modern Aluminum. Walters was injured while operating a belt sander at Modern Aluminum.[48] Walters filed a complaint against Modern Aluminum in state court and Modern Aluminum moved to dismiss the complaint based on the exclusive remedy provision of the Act.[49]

The court noted that for the purposes of the Act, "it is possible for an employee to be 'in the joint service of two (2) or more employers . . . .'"[50] In determining whether Walters was in the joint service of both Kelly Services and Modern Aluminum, the court reiterated the long standing rule that dual employment is found when "both employers possess a substantial, but not necessarily exclusive, right of power or control over the employee and the means, manner, and method of his performance."[51] The court applied the seven factors previously enunciated by Indiana courts[52] to conclude that Walters was in the joint employment of both Kelly Services and Modern Aluminum.[53] Thus, this case merely shows a continuing trend of the court's willingness to apply the

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46. *Id.*
47. 699 N.E.2d 671 (Ind. Ct. App. 1998).
48. *See id.* at 672.
49. *See id.* at 673.
50. *Id.* (quoting IND. CODE § 22-3-3-31 (1998)).
51. *Id.* (citations omitted).
52. The following seven factors were considered:

> (1) the right to discharge; (2) the mode of payment; (3) the supplying of the tools or equipment; (4) the belief of the parties in the existence of an employer-employee relationship; (5) the control over the means used in the results reached; (6) the length of the employment; and (7) the establishment of the work boundaries.

Id. at 674 (citing Fox v. Contract Beverage Packers, Inc., 398 N.E.2d 709, 711 (Ind. Ct. App. 1980)). The court further noted that only a majority of the factors need to be present in order to establish an employer-employee relationship. *Id.* at 675 (citing Davis v. Central Rent-A-Crane, Inc., 663 N.E.2d 1177, 1179 (Ind. Ct. App. 1996)).

53. *Id.* at 675.

seven-factor test in determining whether an employee is in the "joint service of two or more employers" as contemplated by the Act.

C. Coble v. Joseph Motors, Inc.

Psychological injuries and emotional distress have become hotly contested issues in recent times. In *Coble v. Joseph Motors, Inc.*,[54] an employee severed the tip of her left index finger in a press machine while working for Joseph Motors. She was immediately taken to the hospital and treated for her injuries. Meanwhile, the tip of her finger was placed in a plastic bag for disposal.[55] The following day, Coble's fingertip found its way to the desk of the Human Resources Manager, who reportedly displayed the fingertip and made comments to other employees and Coble.[56] Coble brought an action for intentional infliction of emotional distress and outrageous conduct based on the manager's conduct.[57] "The trial judge dismissed Coble's claim for lack of subject matter jurisdiction based upon the exclusivity provision of the [Act]" and granted summary judgment in favor of the employer.[58] Coble appealed this decision.

Most importantly, the Indiana Court of Appeals held that the emotional distress did not constitute a "personal injury" within the meaning of the Act and, therefore, an employee could maintain an action against an employer for intentional infliction of emotional distress.[59] However, the employee must still show that, as an intentional act, the employer had actual knowledge that an injury was certain to occur. Thus, the court of appeals affirmed the trial court's grant of summary judgment because Coble failed to establish that Joseph Motors, or its alter ego, had knowledge that an injury was certain to occur.[60]

V. Election of Remedies

In *Williams v. Delta Steel Corp.*,[61] an employee was injured while working on a machine designed to roll steel into coils. Shortly thereafter, the employee signed a Form 1043 "Agreement to Compensation of Employee and Employer." The Worker's Compensation Board approved the agreement and the employee began receiving disability benefits accordingly.[62] The employee then filed a complaint in state court alleging that the employer knew the machine would cause injury and, therefore, the claim was exempt from the Act's exclusive remedy provision because the injury was intentional.[63]

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54. 695 N.E.2d 129 (Ind. Ct. App. 1998).
55. *See id.* at 131.
56. *See id.*
57. *See id.*
58. *Id.* at 132.
59. *Id.* at 133.
60. *Id.* at 135.
61. 695 N.E.2d 633 (Ind. Ct. App. 1998).
62. *See id.* at 634.
63. *Id.*

The court held that the compensation agreement signed by the employee constituted an election of remedies by the employee and that:

> by accepting and receiving compensation under the Act, [the employee] concedes that the injury was accidental in nature and that it arose out of and in the course of employment . . . the employee is precluded from repudiating that position by claiming that his injury was not accidental but was instead caused by the employer's intentional acts.[64]

The court further explained that "[t]he election of remedies doctrine naturally flows from the exclusivity provision of the Act"[65] and that the provision is part of a "quid pro quo,"[66] wherein "'sacrifices and gains of employees and employers are to some extent put in balance, for, while the employer assumes a new liability without fault, he is relieved of the prospect of large damage verdicts.'"[67] The court stated that the employee should not benefit from the advantages of the Act and still be able to avail himself to the common law remedies.[68] Thus, this decision should, in effect, make the dismissal of a civil action easier where the employee and employer have signed a Form 1043 and had the agreement approved by the Worker's Compensation Board.

VI. Legislative Amendments

The 1996 legislative session brought about many statutory amendments effective in 1997. Some of the more significant changes included: changes to the prosthetic device replacement provisions; the addition of a bad faith provision; changes to the conditions under which TTD benefits may be terminated; and, increased benefits rates. While there were several 1997 legislative proposals, there were no significant legislative changes that became effective in 1998.

A. Prosthetic Device Amendments

When a compensable injury resulted in the amputation of a body part, the enucleation of an eye or the loss of natural teeth, prior to 1997, an employer was responsible for providing an artificial member, braces or prosthodontics.[69] Employers were previously responsible for replacement or repair of such devices if the replacement or repair was due to medical necessity.[70] Section 22-3-3-4(e) of the Indiana Code now provides that the employer will no longer be responsible for the cost of replacement or repair but only for the cost of furnishing the initial

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64. *Id.* at 635.
65. *Id.* at 636.
66. *Id.*
67. *Id.* (quoting 6 ARTHUR LARSON, LARSON'S WORKER'S COMPENSATION LAW § 65.20, at 12-1 to 12-12 (1997)).
68. *Id.* at 637.
69. *See* IND. CODE § 22-3-3-4(e) (1974) (amended 1979).
70. *See id.*

device. Instead, the replacement or repair of such devices will be paid out of the Second Injury Fund, and the employee may replace or repair such devices for medical necessity and for normal wear and tear.[71]

B. Addition of the Bad Faith Provision

The Act now provides the employee a means of recovery for bad faith. Indiana Code section 22-3-4-12.1 gives the Worker's Compensation Board exclusive jurisdiction to adjudicate whether an employer, a worker's compensation administer or a worker's compensation insurance carrier "has acted with a lack of dilligence, in bad faith, or has committed an independent tort in adjusting or settling the claim for compensation."[72] An employee may recover between $500 and $20,000, "depending upon the degree of cupability and the actual damages sustained."[73] This provision also provides for payment of attorney's fees not to exceed one-third of the amount of the award.[74]

To date, there have been no published opinions construing the definition of "lack of diligence" or "bad faith" under the new provision. However, in practice, practitioners have seen an increase in the number of Applications for Adjustment Claim[75] that now allege "bad faith" pursuant to this statute. For example, failure to investigate, failure to complete forms as required by the Act, failure to provide medical treatment and failure to obtain a PPI rating are all acts that have been alleged to constitute "bad faith." Time will tell whether these and other acts constitute bad faith or lack of diligence under the Act and practitioners look forward with interest to the court's interpretation of these terms.

C. Termination of TTD Amendment

The legislature added language to the third condition under which TTD benefits may be terminated, stating "the employee has refused to undergo a medical examination under section [six] of this chapter or has refused to accept suitable employment under section [eleven] of this chapter."[76]

In practice, an employer terminating benefits for the employee's failure to accept suitable employment should do so with caution. Prior to the termination of benefits, the employer should file a Report of Claim Status, state form 38911, indicating its reason for the benefit termination. In addition, it is wise to send a written letter to the employee explaining that a light duty position is available within the employee's restrictions and that failure to report for said position will

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71. *Id.* § 22-3-3-4(e) (1998). *See also* IND. CODE § 22-3-3-4(f) (1998). This section was added to provide that employers must also replace or repair artificial members, braces, implants, eyeglasses, prosthodontics, or other medically prescribed devices that are destroyed or damaged in a compensable accident after June 30, 1997. *Id.*

72. IND. CODE § 22-3-4-12.1 (1998).

73. *Id.* § 22-3-4-12.1(b).

74. *Id.* § 22-3-4-12.1(d).

75. The Application for Adjustment of Claim is state form 29109 filed by the plaintiff.

76. *Id.* § 22-3-3-7(c)(3).

result in a benefits termination. In practice, it is important that any letter sent regarding benefits termination be as detailed and specific as possible.

D. Increased Benefit Rates

The legislature increased compensation per degree for PPI[77] and provided for annual increases in the average weekly wage.[78] The legislature capped any combination of TTD, TPD, and PTD compensation at 500 weeks,[79] thus overturning the decision in *Lowell Health Care Center v. Jordan*.[80] This provision also establishes a minimum of $75,000 for awards that include PTD.[81]

CONCLUSION

The courts have continued to address many important issues during this survey period and practitioners look forward with interest to the changes the following year will bring.

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77. *See id.* § 22-3-3-10(d)(4).
78. *See id.* § 22-3-3-10(e).
79. *See id.* § 22-3-3-32.
80. 641 N.E.2d 675 (Ind. Ct. App. 1994).
81. IND. CODE § 22-3-3-32 (1998).

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LECTURE

TWENTY-FIRST CENTURY CHALLENGES FOR LAW AND PUBLIC HEALTH*

BARRY S. LEVY, M.D., M.P.H.**

I feel deeply honored and thrilled to receive the McDonald-Merrill-Ketcham Award and to deliver this lecture.

This is my third trip to Indiana in the past eighteen months. I continue to be greatly impressed by the public health activities here at Indiana University and throughout the state.

In preparing for this presentation, I recognized that much of my career has involved legal and legislative aspects of public health—as the state epidemiologist in Minnesota, as director of the Occupational Health Program at the University of Massachusetts Medical School, as a relief worker in a Cambodian refugee camp in Thailand, as a researcher and educator in Central and Eastern Europe, and as a consultant to attorneys on toxic tort cases. In these roles and others, I have been impressed with the importance of the law in public health.

Before addressing some of the specific challenges and opportunities that confront law and public health, I will make some general statements concerning the subject of my presentation.

I. PUBLIC HEALTH

I am often asked, "What is public health?" I respond by describing typical daily activities that have been impacted by public health to make our lives safer and more healthful: drinking clean (and often, fluoridated) water, eating more nutritious meals (even with "Nutrition Facts" printed on packages of processed foods), driving safer and less polluting cars, regularly exercising, working in safer and more healthful workplaces, and, for many of us, having access to high quality, comprehensive health care, including preventive clinical services. All

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* The McDonald-Merrill-Ketcham Lecture, Presented in Indianapolis, Indiana, on October 27, 1998. The McDonald-Merrill-Ketcham Lecture and Award was initiated through a joint bequest to the Indiana University Schools of Medicine and Law—Indianapolis by Dorothy M. Ketcham. The award is designed to bridge the gap between law and medicine through honoring an individual, distinguished in both fields, who will share his expertise with students, faculty, and leaders of the medical and legal professions.

** Dr. Levy is Immediate Past President of the American Public Health Association, an Adjunct Professor of Community Health at Tufts University School of Medicine, and an independent consultant in occupational and environmental health.

of this, and more, is the result of public health. Public health has accounted for about twenty-five of the thirty years of increased life expectancy in the United States since the turn of the century. Most people take all of this for granted—unless there is an outbreak of disease, an increase in the occurrence of some disease or injury, an outbreak of domestic or community violence, or a natural disaster.

When public health is most successful, public health activities—in public health practice, education, research, policy development and implementation, and administration and finance—are all almost invisible.

As stated in a landmark report of the Institute of Medicine in 1988,[1] public health is "what we, as a society, do collectively to assure the conditions in which people can be healthy." It takes a society to practice public health—not just public health professionals. Therefore, we need to assure that the public is in public health. We need to engage the public—a public that is largely ignorant and complacent about public health. However, as a 1996 Harris Poll demonstrated, the vast majority of Americans strongly support public health goals, like control of communicable disease, clean air, clean water, control of toxic wastes, and promotion of healthy lifestyles.

II. The Law

Laws concerning public health, at the national, state, and local level, are designed primarily to protect and promote health, and, at the same time, to ensure the rights of individuals. In various situations, different laws take precedence. Public health legal powers derive from the United States Constitution and the state constitutions. Many states have reasonably well-defined codes of public health that provide a basis for public health practice. Many state and local health officers are not fully aware of all the public health powers that they have—powers that can enable them to take necessary actions. For example, in a city in Massachusetts recently, the public health council realized existing laws enabled it to take actions to support a needle exchange program to prevent transmission of HIV and other pathogens. Many public health laws are enacted and enforced under the state's police powers—something that can cut both ways. Many of us public health professionals do not see ourselves as police officers; indeed when we come across as police officers, we may be undermining the public trust that is so essential for our work.

A prominent textbook on public health[2] outlines eight areas of public health law:

1. Environmental Health Laws.—These deal with food, workplace safety, wastewater disposal, and air pollution. Issues often arise concerning right of entry and compensation—not only compensation to victims who may have been harmed, but also compensation to those whose property may have been taken as

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1. Institute of Medicine, Report by the Comm. for the Study of The Future of Public Health (1988).

2. F. Douglas Scutchfield, M.D. & C. William Keck, M.D., M.P.H., Principles of Public Health Practice (1997).

a result of public health measures.

2. *Laws and Regulations on Reporting (Surveillance) of Disease and Injury.*—These enable public health workers to track disease, to identify disease outbreaks, to identify disturbing disease and injury trends, and to provide the basis for intervention to control disease and injury. Many of these laws and regulations transcend an individual's or a patient's right to privacy. Even though physicians are mandated to report specific diseases and injuries of public health importance, most do not; much disease and injury reporting rests on reporting from state laboratories or other sources of data.

3. *Laws Pertaining to Vital Statistics.*—Birth and death records provide an important basis for much public health work, despite frequent inaccuracies, especially in the cause of death recorded on death certificates.

4. *Disease and Injury Control.*—These laws often focus on prevention of disease and injury at the community level. Many policies and programs on such issues as tobacco and alcohol control—like preventing teenagers from drinking and smoking—pertain to this area of public health law.

5.. *Involuntary Testing.*—These laws provide a basis to determine disease prevalence, such as prevalence of HIV/AIDS in a given community, and to identify those who need treatment or restriction from work. In many jurisdictions, food handlers are tested on a regular basis to determine if they have certain infections that might be spread through food preparation.

6. *Contact Tracing.*—Voluntary in nature, contact tracing has proven to be a very effective and efficient way of controlling diseases, such as tuberculosis and sexually transmitted diseases. It played an important role in the worldwide eradication of smallpox.

7. *Immunization and Mandatory Treatment.*—The book *How Can I Help?*[3] describes a dramatic episode in India during the smallpox eradication campaign: An international immunization team invaded a household in the middle of the night to forcibly vaccinate a family against their will. This episode raises many interesting legal, sociocultural, and public health questions.

In the United States and many other countries, laws that mandate certain immunizations exempt people who have religious objections to immunizations.

We need also recognize that even safe and efficacious immunizations can be fatal to some people who receive them. Approximately one in a million people who receive polio vaccine may actually contract and die from polio.

8. *Personal Restrictions.*—Public health authorities have the right to restrict a person carrying salmonella bacteria from working as a food handler. In the past, public health workers often quarantined people who had contagious diseases of public health significance, such as tuberculosis, before effective drugs were available. Quarantine is a form of isolation; while we believe that we are well beyond the age of quarantine, some people believe that we will need to quarantine in the future those infected with resistant infectious agents that pose public health threats. While quarantine is seldom used in the United States

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3. RAM DASS & PAUL GORMAN, HOW CAN I HELP?: STORIES AND REFLECTIONS ON SERVICE (1985).

today, Cuba has quarantined (isolated from the rest of society) people infected with HIV.

III. The Future

I am often asked, "What will the future of public health be like?" I do not know. None of us know. None of us has a crystal ball.

The reality is that we create the future. The future will be determined by our efforts—collectively, as a society. As Dr. Bill Foege, former director of the Centers for Disease Control and a former president of American Public Health Association, has said, humankind now has the capability to create the kind of future we want. Much, of course, depends on the political and popular will to do so.

IV. Challenges for Law and Public Health

For the rest of my presentation, I will focus on twelve important challenges that will affect law and public health as we move into the Twenty-first Century.

In Chinese, the word for "crisis" has two symbols: One symbol stands for danger, and the other symbol stands for opportunity. In many ways, each of the twelve challenges that I will discuss has dangers and opportunities. How we, as a society, address these challenges will determine what happens in the future concerning law and public health.

A. The Genetics Revolution

Perhaps the most profound impact on law and public health in the Twenty-first Century will be as a result of the genetics revolution. The Human Genome Project, which is determining where all of the 75,000 to 100,000 human genes are located, will be completed ahead of schedule—before the year 2005. Not only will we know where all human genes are located, but we will be well on our way to knowing what many of these genes do—and identifying genes that cause disease or confer a high risk of disease to people who carry these genes. There are many important legal, ethical, social, and other questions related to the genetics revolution that are not being addressed adequately.

In about ten years, it may be easy for many of us to learn the make-up of our genome. It is predicted that each of us will have five to forty abnormal genes that confer a high risk of disease. Who should have access to this information? Your employer? Your state or federal government? Your life insurance company? Your health plan? Family members?

I recently attended a conference where a leading government scientist presented a paper on the interaction of a genetic deficiency with an environmental exposure in causing disease. It was a wonderful presentation from a scientific perspective, but neither the presenter nor anyone in the audience addressed the legal and ethical dimensions of this work. Scientists can no longer just perform research; they must be concerned with the relevant policy and practice issues that evolve from their work.

There are other issues here as well. Should workers be genetically screened before entering certain jobs? Should any such screening be voluntary or

involuntary? Should such screening be mandated in any circumstances? Many difficult questions are not now being adequately addressed.

In this week's issue of *Newsweek*, the feature article reports:

> [R]outine genetic screening early in the next century will [identify] the health risks specific to each individual. . . . [T]hose born in the future will probably not have to sit through so many public-service exhortations about fitness. . . . Instead, doctors will tell them which particular risks they run, and what they have to do to stay alive—including, for example, the nutritional supplements that will do them the most good.[4]

We need to provide public health leadership for this brave new world.

B. Access to Quality Health Care

In the United States, we now have a market-driven system of health care—a system where "services" have been replaced by "products," compassion has all too often been replaced by cost containment, and stakeholders have been replaced by stockholders. As market-driven health care is sweeping the country, access to quality health care is being imperiled. Forty-four million people are uninsured, and one million more people are added to this number each year. And most of the rest of us Americans are underinsured. Look carefully at your own health insurance policy—if you are fortunate enough to have one—and see what it covers and what it does not cover. I will bet it does not cover much, if anything, in dental care, care for mental health disorders, vision care, or podiatric care. It probably limits coverage for many other types of care.

In many other ways, our health care system is also in crisis. People covered by Medicare or Medicaid watch their coverage shrink. For-profit managed care organizations seem not to be interested in serving certain populations once they have amassed one-time windfall profits. The United States is the richest country in the world, but ranks twenty-eighth in infant mortality. Our nation is the only Western democracy without any kind of national health plan or system to assure health care coverage for all.

C. Access to Reproductive Health Services

An important part of ensuring the conditions in which people can be healthy is access to reproductive health services, from sex education to abortion. Access to abortion services is not a reality for many women in this country. In addition, abortion service providers are often harassed—and sometime killed. Access to a wide range of reproductive health services will continue to be an important issue as we move into the Twenty-first Century, involving in part, not only the passage of laws and regulations, but also their full implementation.

D. Alternative Health Care

One-third of the U.S. population uses a variety of services and products in

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4. Jerry Adler, *Tomorrow's Child*, NEWSWEEK, Nov. 2, 1998.

the arena of alternative and complementary health care each year—ranging from chiropractic and massage therapy to vitamins and minerals. These services and products are generally not evaluated for safety or efficacy. The Journal of the American Medical Association recently published a report evaluating therapeutic touch, written by an eleven-year-old girl, to make this point.[5] On a positive note, the relatively new Office of Alternative Medicine at the National Institutes of Health, though woefully underfunded, is striving to evaluate the safety and efficacy of these modalities. In 1997, it held a consensus conference on acupuncture, which promulgated helpful information to practitioners and the public at large. Developing and disseminating this kind of information needs to be done on a much broader scale.

E. Population Changes

The U.S. population is become more diverse and, on average, older. In the United States, diversity has always been our strength. Now we are more culturally diverse than ever before. There are over 100 languages spoken in the schools in Los Angeles, and a surprising number spoken in schools here in Indianapolis and many other places across the country. We need to ensure that health services are available—geographically and culturally—to all people in this country, even people who may be classified as illegal aliens.

The United States has an aging population, as is true in many countries. We need to ensure that health services are available to people of all age groups. The fastest growing age group in the United States is eighty-five and older. By the year 2050, there will be one million people in this country over the age of 100.

Migration between and within countries is another important population issue worldwide. In many of the less-developed countries, young men, in search of jobs, migrate from rural to urban areas, often leaving behind their wives and children at home in the countryside. This type of migration often puts women under great physical and sociocultural stress. Men, who may or may not find jobs in the city, are at high risk of substance abuse, sexually transmitted diseases, and other health problems.

There is also much migration of people between countries—people who often give up their rights as they move from one country to another. Worldwide, fifty million refugees have been uprooted, approximately half of them within the borders of their own countries—as "internally displaced persons," without easy access to food, clothing, shelter, or medical care and other human services. We should be very concerned about the legal issues—global and international legal issues—regarding refugees and their health.

F. The Emergence and Re-emergence of Infectious Diseases

In this area, there are very many important issues, such as issues concerning disease reporting, contact tracing, and confidentiality of information; safety of food and water; increasing resistance of microorganisms to antibiotics; screening

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5. Linda Rosa et al., *A Close Look at Therapeutic Touch*, 279 JAMA 1005 (1998).

of individuals, such as screening pregnant women and/or infants for HIV infection; and imposition of control measures that may infringe on individuals' freedom or corporate profits.

G. The Information and Communication Revolution

There are many opportunities here, such as improved communication with other professionals and the public at large and better ways of gathering, analyzing, and disseminating data. But there are also dangers, such as breaches of confidentiality. For example, my wife, children, and I receive our health care from one of the best health maintenance organizations ("HMOs") in the United States. But three years ago, the *Boston Globe* reported that any employee of that HMO could access by computer any patient's medical data, including psychiatric records. This deficiency was very quickly corrected, but I wonder how many other HMOs across the country have similar lapses in protecting confidential data. These developments raise concerns for the law and public health. We could see a backlash on confidentiality such that public health practitioners and researchers do not have necessary access to data of public health importance.

We in public health and in the law should be concerned about this possible backlash. On one hand, we should ensure appropriate confidentiality of data, but not such confidentiality that people who need access to these data in order to protect the public's health do not have such access.

H. Tobacco

The law has a profound set of impacts on tobacco policies and programs as they pertain to the public's health. Each day, more than 1000 Americans die of tobacco-related disease. Each day, 3000 people begin smoking in the United States—most of them teenagers, some of them fourth-graders. In Indiana, forty-two percent of high school seniors smoke—and the percentage is higher in subgroups of this population. While the overall level of smoking in this country has decreased from about forty percent to about twenty-five percent in the past few decades, the smoking rate has been increasing among teenagers and other subgroups of the population.

For every person in the United States who quits smoking, approximately three people in other countries start smoking American tobacco. No surprise then that the tobacco industry is willing to agree to settlements of lawsuits here in the United States, as long as these settlements do not interfere with tobacco sales abroad. In Vietnam and some countries in the Middle East and Central and Eastern Europe, more than two-thirds of adults smoke. Thailand, recognizing the human and economic adverse effects of cigarettes, resisted for many years the import of American tobacco. Under great pressure from the United States and ultimately the World Trade Organization, Thailand was forced to relent and to import American tobacco. Tobacco will clearly continue to be an important public health issue in the Twenty-first Century on which those of us in law and public health need to continue to work closely together.

I. Violence

The United States has the highest rate of gun-related fatalities in the world—more than four times higher than the country with the second highest rate. Gun-related violence is both a public health issue and a legal issue.

There are approximately twenty-five civil wars taking place during 1998, as there have been in each year of the 1990s. During this decade, civilian deaths have accounted for 90 percent of all war-related fatalities—many of them women and children. There are a number of international legal issues here, such as when it is right for the global community to intervene in a civil war. We said that we learned a lesson from the Holocaust: Never again. Then came the Cambodian genocide, the Rwandan genocide, and other mass killings in which no external force intervened until it was too late.

J. Chemical Hazards in the Workplace and the Ambient Environment

There are approximately 80,000 chemicals in commercial use, with about 1000 more added each year. Approximately 15,000 of these are in widespread commercial use. In this arena, development and implementation of laws and regulations has led to important progress. As a result of the Toxic Release Inventory, for example, companies provide to the public information on what they are emitting into the air and water in their communities. Right-to-know legislation at the state and federal level, starting in the 1970s, has had a profound impact on enabling workers and community residents to know to what substances they are being exposed. Yet relatively few of the approximately 80,000 chemicals in commercial use have been adequately evaluated for adverse health effects. Relatively little research has been performed on protecting vulnerable populations from chemical hazards. Many laws and regulations are designed to protect most people in the community—but not necessarily infants and children, senior citizens, pregnant women, people who are immunocompromised, those with certain health conditions, those on certain medications, and those who are at heightened risk of adverse health effects from chemicals for other reasons. We need to improve how we control chemical hazards in both the workplace and the ambient environment.

K. The Export of Hazards

The United States and other more-developed countries export to less-developed countries many hazardous substances, including pesticides, tobacco, and dangerous pharmaceutical products. Many of these substances have been banned for sale in the United States and other more-developed countries, which have limited, if any, restriction on their export and sale elsewhere.

I have consulted to plaintiffs' attorneys on an international situation involving the export of the pesticide dibromochlorpropane ("DBCP") from the United States to many less-developed countries. DBCP was banned in the United States in the late 1970s because it was then demonstrated to cause sterility in men. For the purpose of a lawsuit against American companies that had been exporting DBCP to those countries after it was banned in the United States, these attorneys identified more than 26,000 men in these countries who had evidence

of sterility or reduced fertility. Although the companies were fully aware of the hazards of DBCP, these men, who applied DBCP on banana and pineapple plantations, were not at all aware of these hazards. The adverse health impacts of the export of hazardous substances on people in less-developed countries, I believe, are widespread and serious. But these problems are rarely detected for a number of reasons—inadequate access to medical care; inadequate or nonexistent systems for surveillance of disease and for research; workers so desperate for jobs and nations so desperate for economic development that they are willing to overlook health hazards; and the presence of even more serious health problems, like malaria, AIDS, and waterborne diarrheal disease, in these countries.

The United States even exports entire hazardous industries. For example, some U.S. industries have moved their plants a short distance from southern states across the border to Mexico, where occupational and environmental laws and regulations are less stringent, and where workers' pay and benefits are far less than they are in the United States.

L. Global Public Health Issues

These issues, including global warming and the depletion of the stratospheric ozone layer, deal with how well we protect the global commons.

Vice President Al Gore would like the United States to launch a satellite that would constantly beam a televised image of the earth in order to constantly remind us of the preciousness and fragility of our planetary environment and our need to conserve nonrenewable resources and to reduce pollution of our air, water, and soil.

International agreements on global environmental protection, such as the 1997 Kyoto Agreements to limit emissions of greenhouse gases and thereby reduce global warming, offer some hope. But the euphoria that accompanied the signing of the agreements ten months ago has dissipated as nations now contemplate the challenges of implementing them.

The world of the Twenty-first Century is likely to be heavily impacted by trade agreements. The ability of national governments to regulate air pollution, water pollution, and occupational health and safety may be seriously weakened as regional and global trade agreements are developed and implemented.

V. RELATED ISSUES

These twelve sets of challenges should not overwhelm us. We need not become experts in all twelve areas. But we must understand the dangers and the opportunities that these challenges represent for law and public health as we move into the Twenty-first Century.

There are other important issues intimately connected with the twelve challenges.

A. Campaign Financing

On Election Day, next Tuesday, we may elect the best Congress that money can buy. Not only does money too often buy election victories, but also our

legislators are spending increasingly more time fundraising. The average Congressperson attends three fundraising events daily—just to raise money for the next election campaign. Campaign finance reform at the national and state level is a critically important issue for the law and public health.

B. Control of the Mass Media

Should a tobacco company own a newspaper chain? Should a firearms company own a television station? There are important legal, ethical, and public health issues concerning ownership and control of the mass media. The current situation in which a few large conglomerates control the mass media in the United States can be inimical to the goals of public health.

C. Underlying Factors

Virtually all public health problems have underlying social and cultural factors and abrogations of human rights that contribute to their causation. This is the fiftieth anniversary year of the signing of the Universal Declaration of Human Rights ("UDHR"). One of the thirty articles in the UDHR states that people should have their basic health rights protected. The late Dr. Jonathan Mann, founding director of the Global Program on AIDS of the World Health Organization, concluded that the AIDS pandemic was a result not only of HIV transmission, but also the abrogation of human rights. In championing the relationship between health and human rights, he asserted that the UDHR provides a coherent framework and systematic approach to identify and ensure the conditions in which people can be healthy—in other words, a framework and approach to ensure the goal of public health.

Article 25 of the UDHR states all people should have their basic human rights protected:

> Everyone has a right to a standard of living adequate for the health and well-being of [oneself] and [one's] family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond [one's] control.

If we use Article 25 of the UDHR as a yardstick to assess how our global society is doing, we are falling way short.

Legal and public health professionals can do much to assure that basic human rights are protected and, in turn, that we as a society, assure the conditions in which people can be healthy.

VI. WHAT WE NEED TO DO

A. Listen

We need to think globally but act locally. First, however, we need to go out and listen to the people in the communities that we serve in order to understand their needs better.

B. Educate

We need to educate ourselves and our colleagues, and people throughout society on the issues discussed today and other important issues of law and public health, because it takes a society—an informed and educated society—to practice public health.

C. Advocate

We need to advocate for assuring the conditions in which people can be healthy. If we do not advocate for these conditions, and the basic human rights on which they are based, perhaps no one else will. We need to be more effective advocates for public health.

D. Collaborate

We need to collaborate to form broader partnerships between ourselves and others in the community in order to achieve the goal of public health. We need to ensure that the public is engaged in public health.

VII. WHO WE NEED TO BE

A. Values

Values are what brought many of us into the careers for which we are studying or in which we are practicing at the present time. Values such as equity, integrity, human dignity, prevention of disease and injury, and protection of human rights—these and other values are essential for public health. They are the basis of many public health laws and regulations. They are the basis of our state and national constitutions. If we do not articulate these values, perhaps no one else will.

There is a crisis of values in our nation today, as poet and author Marianne Williamson and others have asserted. She has stated that we, as a nation, "comfort the comfortable and afflict the afflicted." Data show that the rich are getting richer, and the poor poorer. The richest one-fifth of people worldwide own eighty-five percent of the wealth; the poorest one-fifth of people own one percent of the wealth. The gaps between the rich and poor countries have doubled in the past thirty years. The gaps between the rich and the poor in this country are as wide as they have ever been.

We need to articulate our public health values and assure that they are embodied in laws and regulations that are passed and implemented.

B. Vision

Also critical to the future of law and public health is vision. Were it not for people with visions fifty years ago, we would not be on the brink of worldwide polio eradication today. Were it not for people with visions twenty-five years ago, we would not have progressive smoking policies today—we might not be meeting in a smoke-free facility. We need to have visions—even seemingly

impossible visions. As Robert Kennedy said, "Some people see things as they are and ask, 'Why?' I dream things that never were and ask, 'Why not?'" We need to dream things that never were and ask, "Why not?"

C. Leadership

We need to have leadership to translate these values and visions into reality. Each and every one of you and your colleagues are leaders in law and public health—leaders with expertise, commitment, and courage—leaders who not only do things right, but who also choose to do the right things.

I recently told a visiting professor from England to Tufts Medical School, where I have an adjunct faculty appointment, that we in public health in this country are having a difficult time getting a seat at the managed care table. He laughed and said, "We in public health in England see ourselves as the table." We in the law and public health in the United States need not always fight to get a seat at the table where decisions are being made. Instead, we need figuratively to be the table. We often have the legal and legislative mandate to be the table. We must ensure that public health decisions should be made in a public health framework—a framework that includes participation by people from not only the law and from the public health professions, but from all of society. We in the law and public health should be framing issues, obtaining and analyzing relevant data, and bringing people from all segments of society together to discuss issues and make societal decisions—decisions about public health. Being the table is a key element of leadership.

We leaders may not see the impact of our leadership during our lifetimes, and we may not receive the appreciation and acknowledgment that we may think we deserve. But our true acknowledgment ultimately will be in how well the goals for which we are striving are adopted by our communities, locally and globally. As is stated in a wonderful poem, which was written 2500 years ago by Lao Tsu:

> Go to the people,
> Learn from them,
> Love them,
> Start with what they know,
> Build on what they have;
> But of the best leaders,
> When their task is accomplished,
> Their work is done,
> The people will remark,
> "We have done it ourselves."

The values, vision, and leadership that we in the law and in the public health professions provide will help bring about the true goal of public health—assurance of the conditions in which people can be healthy.